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TABLE OF CASES CITED.

IN THE

Supreme Court of the United States.

OCTOBER TERM, 1921.

No. 610.

SEWARD PROSSER, MORTIMER N. BUCKNER and JOHN H. MASON, as a Committee, etc.,
Appellants,
vs.
READING COMPANY, *et al.*,
Appellees.

BRIEF FOR APPELLANTS.

Statement of the Case.

This is an appeal from a decree (Transcript of Record, p. 287) of the District Court of the United States for the Eastern District of Pennsylvania, filed June 6, 1921, in the cause enttiled "The United States of America, Petitioner, *vs.* Reading Company, *et al.*, Defendants." The appellants Seward Prosser, Mortimer N. Buckner and John H. Mason are a Committee representing holders of common stock of defendant Reading Company, and, as such Committee, became intervening parties defendant in

the aforesaid cause under the circumstances hereinafter set forth.

The capital stock of Reading Company consists of

560,000 shares of First Preferred Stock of par value of	$28,000,000
840,000 shares of Second Preferred Stock of a par value of	42,000,000
1,400,000 shares of Common Stock of a par value of	70,000,000

aggregating 2,800,000 shares of a par value of $50 each and a total par value of $140,000,000 (Transcript, pp. 102, 157).

The New York Central Railroad Company, one of the appellees herein, is the owner of 121,300 shares of First Preferred, 285,300 shares of Second Preferred, and 197,050 shares of Common stock (Transcript, p. 140), and The Baltimore and Ohio Railroad Company, another of the appellees herein, is the owner of 121,300 shares of First Preferred, 285,300 shares of Second Preferred, and 200,050 shares of Common stock (Transcript, p. 142). Thus their combined ownerships aggregate,

813,200 shares, or 58% of the 1,400,000 shares of the Preferred stocks,
397,100 shares, or 28% of the 1,400,000 shares of the Common stock, and
1,210,300 shares, or 43% of the 2,800,000 shares of stock of all classes;

and their interests in the Preferred stocks aggregate more than twice their interests in the Common stock.

The appellants represent 2,629 holders of 407,728 shares of the Common stock. Of these holders 462 own less than 10 shares, 1,362 own less than 25 shares, 1,644 own less than 50 shares, 1,931 own less than 100 shares and 698 own 100 shares or more (Transcript, p. 208). Their holdings constitute 29 per cent. of the total of 1,400,000 shares of Common stock and 41 per cent. of the

1,002,900 shares thereof not owned by the two railroad companies, as aforesaid.

This appeal brings up for determination the respective rights of the holders of the Preferred stocks and the holders of the Common stock of Reading Company in and to the interest of the Reading Company in The Philadelphia & Reading Coal & Iron Company upon the disposition of such interest by Reading Company pursuant to the mandate (Transcript, p. 27) of this Court filed in the District Court ~~of~~ in the cause entitled "The United States of America, Petitioner, *vs.* Reading Company, *et al.*, Defendants." At the conclusion of the further proceedings upon said mandate in the District Court a final decree (Transcript, p. 287) was filed therein on June 6, 1921, and from that decree this appeal is taken.

The parties to this appeal, their relations to the subject-matter thereof and to each other, the questions involved therein and the manner in which they are raised, will appear from the following chronological account of the proceedings that resulted in the final decree from which this appeal is taken.

The Segregation Proceedings.

The cause entitled "The United States of America, Petitioner, *vs.* Reading Company, *et al.*, Defendants" was a suit instituted by the Government in 1913 against the Reading Company and certain affiliated corporations to dissolve the intercorporate relations existing between the corporation defendants, for the reason that through such relations they constituted a combination in restraint of interstate commerce in anthracite coal, and an attempt to monopolize or a monopolization of such trade and commerce, in violation of the first and second sections of the Anti-Trust Act of Congress, of July 2, 1890, Chap. 647, 26 Stat. 209; and also for the reason that the defendants, Philadelphia & Reading Railway Company and Central

Railroad Company of New Jersey were violating the commodities clause of the Act of Congress of June 29, 1906, Chap. 3591, 34 Stat. 585, by transporting over their lines of railroad, in interstate commerce, coal mined or purchased by coal companies with which they were associated by stock ownership. Pursuant to the provisions of the Act of June 25, 1910, Chap. 428, 36 Stat. 854, commonly known as the Expediting Act, the then Attorney-General of the United States certified the general public importance of the controversy, and the cause was thereupon heard by three Circuit Judges of the Third Circuit. The decree was filed on October 28, 1915, appeals wherefrom were taken to this Court by both the Government and by the defendants.

Those appeals were decided by this Court in the October Term, 1919. This Court held, among other things, that the control by Reading Company of The Philadelphia & Reading Coal & Iron Company and the Philadelphia and Reading Railway Company constituted a combination in violation of the Anti-Trust Act of July 2, 1890, as well as of the commodities clause of the Act of June 29, 1906; affirmed in part and reversed in part the decree filed on October 28, 1915, and remanded the cause to the District Court with direction to enter a decree in conformity with the opinion of this Court (*United States* v. *Reading Company et al.*, 253 U. S. 26; Transcript, p. 1).

Upon the mandate (Transcript, p. 27) of this Court dated June 15, 1920, and filed in the District Court on August 13, 1920, the District Court filed on October 8, 1920, an interlocutory decree (Transcript, p. 31) which provided for the dissolution of the combination declared to be unlawful, by directing that "the defendants shall submit to this Court a plan for the dissolution of the unlawful combination between the Reading Company, the Philadelphia and Reading Railway Company, the Philadelphia & Reading Coal and Iron Company, the Central Railroad Company of New Jersey and the Lehigh

& Wilkes-Barre Coal Company, existing and maintained through the Reading Company, with such provision for the disposition of the shares of stock and bonds and other property of the various companies, held by the Reading Company, as may be necessary to establish the entire independence from that company and from each other, of the Philadelphia & Reading Railway Company, the Philadelphia and Reading Coal & Iron Company, the Central Railroad Company of New Jersey and the Lehigh & Wilkes-Barre Coal Company, to the end that the affairs of all these now combined companies may be conducted in harmony with the law" (Transcript, pp. 36, 37).

Pursuant to such direction, the defendants, Reading Company, Philadelphia and Reading Railway Company and The Philadelphia & Reading Coal & Iron Company, submitted to the District Court on February 14, 1921, a Plan (Transcript, p. 40) the proposals of which, so far as they are connected with this appeal, were in substance:

1. The Reading Company would assume the $96,524,000 General Mortgage 4% bonds, being a joint obligation of Reading Company and The Philadelphia & Reading Coal & Iron Company (hereinafter called the "Coal Company"), and would agree to save the Coal Company and its property harmless therefrom (Transcript, p. 41).

2. The Coal Company would pay to Reading Company $10,000,000 in cash, or current assets at market value, and $25,000,000 in 4% mortgage bonds of the Coal Company, to be issued under a new mortgage and to mature on January 1, 1997, the same date as the General Mortgage bonds (Transcript, p. 41).

3. General releases of all claims and liabilities as between Reading Company and the Coal Company, including the claim of approximately $70,000,000 carried on the books of Reading Company as an

asset and on the books of the Coal Company as a liability, would be exchanged (Transcript, p. 41).

4. The Reading Company would agree that it would obtain the release of the coal property from the lien of the General Mortgage and the discharge of the Coal Company from liability on the General Mortgage bonds, provided such release and discharge could be secured by payment by Reading Company to the bondsholders of a premium not exceeding 10% upon the par value of the outstanding General Mortgage bonds (Transcript, pp. 41, 42).

5. It was assumed that the Attorney-General would ask the Court to direct the release of the stock of the Coal Company from the lien of the General Mortgage on such terms as the Court might fix. If practicable, the Coal Company would consolidate with Delaware Coal Company, of which it owns the entire capital stock, and the consolidated company would issue stock without par value to Reading Company. If that were not practicable, a new corporation would be created to acquire from Reading Company the stock of the Coal Company, or the interest of Reading Company therein, and such new corporation would issue no par value stock. The number of shares to be issued of the consolidated Coal Company or such new corporation might be 1,400,000.

Such no par value stock would be sold to the stockholders of Reading Company, preferred and common, share and share alike, for $5,600,000, or $2 for each share of Reading stock. It was proposed to carry out this sale, in accordance with the precedent established by the Union Pacific-Southern Pacific case, by distributing to Reading stockholders assignable certificates of interest in the Coal Company stock exchangeable for such stock only when accom-

panied by an affidavit that the holder was not the owner of any stock of Reading Company. Any further steps which might be deemed necessary by the Court would be taken to the end that an independent board and management, to be approved by it, would be maintained for the Coal Company so that the independence of this company need not await the necessarily gradual process of the distribution of the stock of the Coal Company among persons not holders of stock in Reading Company (Transcript, pp. 42, 43).

6. The Reading Company would merge the Philadelphia & Reading Railway Company under the authority contained in the present charter of the Reading Company and would subject the Railway property to the direct lien of the General Mortgage. The name of Reading Company, after merger, would not be changed. The Reading Company would accept the Pennsylvania Constitution of 1874, and would proceed under the Act of 1856 to surrender those of its powers which are inappropriate for a railroad corporation of Pennsylvania. Thus, Reading Company would be in all respects subject to the regulation of State and Federal authorities as a common carrier, and the relation of Reading Company, as a specially chartered holding company, to the Philadelphia and Reading Railway Company would be terminated (Transcript, pp. 43, 44).*

* Paragraph 7 of said Plan (Transcript, p. 44) dealt with a proposed refunding and improvement mortgage to be executed by Reading Company, and paragraph 8 thereof (Transcript, pp. 44, 45) dealt with the sale of the stock held by Reading Company in The Central Railroad Company of New Jersey and the sale of the stock held by The Central Railroad Company of New Jersey in Lehigh and Wilkes-Barre Coal Company. None of these matters is involved in this appeal.

At the time of the submission of said Plan the Government submitted to the District Court a Counter Proposal (Transcript, p. 45) which dealt only with paragraph 8 of said Plan, and is, therefore, not involved in this appeal.

Upon the submission of said Plan and Counter Proposal, the District Court made an order (Transcript, p. 46), filed on February 14, 1921, which directed that copies thereof be served on Central Union Trust Company of New York, the trustee under the General Mortgage referred to in said Plan, and be filed in the office of the Clerk of the District Court and at the offices of Reading Company in Philadelphia and New York, to be open to the inspection of all stockholders of the defendant companies; and, further, set for March 1, 1921, a hearing at which the Attorney-General and counsel for the defendants would be heard further on the Proposed Plan and in regard to the subject-matter thereof.

Copies of said Plan and Counter Proposal having been served and filed as directed by said order, the Government filed on March 1, 1921, a supplemental bill (Transcript, p. 48) to make Central Union Trust Company of New York a party to the cause, for the reason that said Plan provided, among other things, for the release of the stock of the Coal Company from the lien of the General Mortgage referred to in said Plan, and also for the release of all the property of the Coal Company from the lien of said Mortgage and the assumption of the entire obligation thereof by Reading Company (Transcript, p. 49, par. 5).

Immediately after said Plan and Counter Proposal became open to the inspection of the stockholders of Reading Company, the appellants, at the request of certain holders of common stock of Reading Company, formed themselves into a committee for the purpose of examining said Plan and representing and protecting the interests of such stockholders in connection therewith.

After examining the same the appellants concluded that in the formulation thereof the interests of the holders of common stock of Reading Company had been over-

looked and neglected by the Board of Directors of the Reading Company and that the effect of carrying out such Plan was to distribute to the preferred stockholders, ratably per share with the common stockholders, a surplus of upwards of $33,000,000 accumulated by Reading Company from the undivided net profits arising from its business, whereas, in fact and in law, and in compliance with the contract between the holders of the first and second preferred stocks and the holders of the common stock, practically all of said surplus belonged, under the circumstances there obtaining, to the holders of common stock, to the exclusion of the holders of both classes of preferred stock. Acting upon this conclusion, they prepared a petition (Transcript, p. 96) for leave to intervene and suggesting modification of the Plan, which was verified February 28, 1921, and an amended and supplemental petition (Transcript, p. 101) for modification of the Plan, which was verified on March 14, 1921, both of which petitions were filed on March 15, 1921.

Continental Insurance Company and Fidelity-Phenix Fire Insurance Company of New York, holders of common stock of Reading Company, also prepared a petition (Transcript, p. 51) for leave to intervene, verified March 12, 1921, wherein they raised substantially the same objections to said Plan as were raised in the petitions of the appellants.

Frances T. Ingraham and others, owners of common stock of Reading Company, by a petition (Transcript, p. 120), verified March 14, 1921, asked for information from Reading Company as to the value of their interest in the property thereof.

The following parties filed petitions for leave to intervene in support of said Plan:

Adrian Iselin, Robert B. Dodson, Edwin G. Merrill and William A. Law, as a committee representing certain holders of first and second preferred stock of Reading Company (Transcript, p. 131);

William B. Kurtz and Madge Fulton Kurtz, owners of 5,100 shares of second preferred stock of Reading Company (Transcript, p. 143);

The New York Central Railroad Company, owner of 406,600 shares of first and second preferred stock and 197,050 shares of common stock of Reading Company (Transcript, p. 140);

The Baltimore and Ohio Railroad Company, owner of 406,600 shares of first and second preferred stock and 200,050 shares of common stock of Reading Company (Transcript, p. 142).

The following parties filed petitions for leave to intervene by reason of their ownership of certain of the General Mortgage bonds referred to in said Plan:

Penn Mutual Life Insurance Company (Transcript, p. 144);

The Pennsylvania Company for Insurances on Lives and Granting Annuities (Transcript, p. 146).

The Girard Avenue Title and Trust Company, owner of 900 shares of common stock and of $15,000 principal amount of said General Mortgage bonds, also filed a petition for leave to intervene (Transcript, p. 145).

Joseph E. Widener filed a petition (Transcript, p. 148) for leave to intervene and to present a separate answer to certain of the intervening petitions and cross petitions that had been filed, in which he set forth that he was a member of the Board of Directors of Reading Company; that, as actual owner and as trustee of the estate of P. A. B. Widener, his father, his combined holdings of common stock of Reading Company were over 100,000 shares; that, as a member of the Board of Directors of Reading Company, he had approved, and still approved, said Plan, and that, while he had originally given to the appellant committee his power of attorney with respect to the common stock of Reading Company held by him, he had felt constrained to with-

draw that power and to support said Plan by reason of his belief that the questions of construction of the contracts between the different classes of stockholders and Reading Company that had been raised were not in any way involved in the proceeding.

Central Union Trust Company of New York, on April 12, 1921, filed its answer (Transcript, p. 150) to the supplemental bill (Transcript, p. 48) of the Government, wherein it prayed that no decree should be entered that would in any wise disturb the General Mortgage referred to in the Plan, or the lien thereof, or any security thereunder, or the security of the holders of bonds secured by said mortgage, as in said mortgage provided, and that any decree entered should recognize the unimpaired validity of said mortgage and the lien and pledge thereby created (Transcript, p. 152).

The defendant Reading Company, on April 5, 1921, filed its answer to intervening petitions and cross petition (Transcript, p. 153), in which it defended said Plan against the objections thereto that had been made in the petitions by these appellants and by Continental Insurance Company and Fidelity-Phenix Fire Insurance Company of New York.

By an order (Transcript, p. 203), filed April 12, 1921, the District Court gave leave to intervene to all of the parties who had filed the aforesaid petitions, and all of said parties duly filed their appearances (Transcript, p. 207). Such of said parties as appeared in a representative capacity, as a committee or otherwise, also duly filed the certificates required of them by said order as a condition to their intervening (Transcript, p. 208).

By a further order (Transcript, p. 205), filed on April 12, 1921, the District Court, being of opinion that certain matters presented in the petitions of the intervenors in relation to the said Plan should be considered further by the Court only after hearing of the parties of record in

the cause, decreed that on May 2, 1921, it would hear argument upon the following questions:

> (1) (*a*) Whether the sale provided for in paragraph Five of the Reading Plan is such a disposition of the interest of Reading Company in the stock of The Philadelphia & Reading Coal & Iron Company as accomplishes the express purpose of the mandate of the Supreme Court of the United States requiring disposition by Reading Company of such stock because the holding of it has been and would be unlawful; (*b*) and if the mandate is thereby complied with, whether such disposition confers upon any one class of stockholders of Reading Company any benefit to the prejudice of the legal rights of any other class of stockholders.
>
> (2) Whether the stock of the Coal Company should be sold free from the lien of the General Mortgage, or whether a sale of Certificates of Interest therein would be a compliance with the provisions aforesaid of the mandate of the Supreme Court of the United States.
>
> (3) Whether the Reading Company should offer a premium of ten per cent. to the General Mortgage bondholders for release of the Coal Company's property from the lien of the mortgage, or whether the requirements of the mandate of the Supreme Court of the United States may be fulfilled by proper injunctive provisions in the decree to be entered in this cause.

After argument of said questions, the defendant Reading Company, pursuant to direction of the Court at the hearing, submitted certain modifications of said Plan (Transcript, p. 210) which were designed to meet only the objections that had been made on the argument by Central Union Trust Company of New York, as Trustee of the General Mortgage referred to in said Plan, and by the intervening holders of bonds secured by said mortgage.

The Plan as modified (Transcript, p. 274) was approved by an opinion (Transcript, p. 278) of the District Court, filed May 21, 1921, and, in conformity with said opinion, a decree (Transcript, p. 287) was filed in the District Court on June 6, 1921. From that decree this appeal is taken (Transcript, pp. 332, 333, 338, 339).

The Reading Company.

The Reading Company was incorporated as "Excelsior Enterprise Company" on May 24, 1871, by a special act of the Legislature of Pennsylvania, which act is set forth in full in the record (Transcript, p. 189).

The act provided that the corporation should have, enjoy and exercise the same rights, powers, privileges, franchises and immunities as were conferred by an act entitled "An Act to incorporate the Pennsylvania Company", approved April 7, 1870, and as were conferred by any then existing supplements to the charter of the Pennsylvania Company (Transcript, p. 190, Section 2).

This has the effect of bringing into the charter of the Reading Company the charter of the Pennsylvania Company, as set forth in the act approved April 7, 1870 (Transcript, pp. 190-196), and an act supplementary thereto approved February 18, 1871 (Transcript, pp. 196, 197).

From these three acts, taken together, it appears that Reading Company has "the power to make purchases and sales of or investments in the bonds and securities of other companies, and to make advances of money and of credit to other companies, * * * and to receive and hold, on deposit or as collateral, or otherwise, any estate or property, real or personal, including the notes, obligations and accounts of individuals and companies, and the same to purchase, collect, adjust and settle, and also to pledge, sell and dispose thereof, on such terms as may be agreed on between them and the parties contracting

with them" (Transcript, p. 192), and that there is no limitation upon its corporate powers except that "nothing herein contained shall be so construed as to give to the said corporation any banking privileges or franchises, or the privileges of issuing their obligations as money" (Transcript, p. 191).

This charter does not set forth any of the terms of the stock contract among the stockholders and between the stockholders and the corporation, and the only provisions of the charter that relate to the capital stock and that require consideration here are the following:

> "The capital stock of said company shall consist of two thousand shares of the value of fifty dollars each, being one hundred thousand dollars, and with the privilege of increasing the same, by a vote of the holders of a majority of the stock present at any annual or special meeting, to such an amount as they may from time to time deem needful" (Transcript, p. 194).
>
> "should the capital stock at any time be increased, the stockholders, at the time of such increase, shall be entitled to a *pro rata* share of such increase, upon the payment of the instalments thereon duly called for;" (Transcript, p. 194).
>
> "That the capital stock of said company as authorized by said act, or the stock thereof when increased in the mode and manner prescribed therein, may be in the whole common, or in part preferred stock, as the said company may from time to time determine;" (Transcript, p. 196).

It is also provided:

> "That the stockholders of the said company, by and with the advice and consent of the holders of two-thirds of the shares of stock, be and they are hereby authorized to change the name and title of the said company," (Transcript, p. 190).

The terms and conditions of the stock contract must, therefore, be found in the stock certificates themselves.

The Reading Company is not a common carrier, and is not subject to regulation by Federal or State authorities having jurisdiction of railroads (Transcript, p. 157).

Prior to 1896 the Reading Company was an inactive corporation, with an authorized capital stock of $100,000, whose charter had been kept alive and was in the possession of The Philadelphia and Reading *Railroad* Company (hereinafter called the "Railroad Company"). In that year a reorganization of the properties of the Railroad Company and The Philadelphia and Reading Coal and Iron Company (hereinafter called the "Coal Company") became necessary by reason of the foreclosure of the General Mortgage of said companies (Transcript, p. 158).

The reorganization plan dated December 14, 1895, provided for an issue of general mortgage bonds, preferred stock and common stock, as follows:

"1. General Mortgage 100-year 4% Gold Bonds.

* * * * * *

"2. Non-cumulative 4% First Preferred Stock for $28,000,000, subject to an increase of $21,000,000, as hereinafter stated, for substitution for Second Preferred Stock. The First Preferred Stock will entitle the holders to non-cumulative dividends up to 4% per annum, payable out of net earnings before any dividends shall be paid on the Second Preferred or the Common Stock.

"3. Non-cumulative, 4% Second Preferred Stock for $42,000,000, which will entitle the holders to non-cumulative dividends up to 4% per annum, payable out of net earnings before any dividends shall be paid on the Common Stock.

"4. Common Stock for $70,000,000, subject to an increase of $21,000,000, as hereinafter stated, for substitution for Second Preferred Stock.

* * * * * *

"Provision will be made that at any time after dividends at the rate of 4 per cent. per annum shall have been paid for two successive years on the First Preferred Stock, the New Company may convert the

Second Preferred Stock at par, one-half into First Preferred Stock and one-half into Common Stock" (Transcript, p. 159).

The properties formerly of the Railroad Company and the Coal Company were sold under foreclosure to purchasers who acted by arrangement with the reorganization managers. The capital stock of Reading Company was increased to provide for the issue of the preferred stocks and common stock set forth in the reorganization plan; and such stocks and $50,369,000 principal amount of General Mortgage bonds were issued against the acquisition of the properties of the Railroad Company and the Coal Company and were exchanged for outstanding securities of the Railroad Company or sold to provide the cash necessary for organization purposes (Transcript, pp. 159, 160).

In the consummation of the reorganization plan the Reading Company became the owner of $8,000,000 par value, being all, of the capital stock of the Coal Company and the owner of all of the capital stock of the new Philadelphia & Reading *Railway* Company, which had succeeded to most of the properties of the Railroad Company. The Reading Company and the Coal Company became joint obligors of the General Mortgage and the bonds issued thereunder (which are referred to in the Plan as modified, out of which this appeal arises) and the stocks of the Coal Company and the Railway Company, as well as the properties of the Coal Company, were subjected to the lien of said General Mortgage (Transcript, pp. 157, 158).

The preferred stocks and common stock, as provided for in the reorganization plan, were issued by Reading Company in the form shown by the certificates of the first preferred stock (Transcript, p. 88), second preferred stock (Transcript, p. 90) and common stock (Transcript,

p. 92), to which certificates resort must be had for the terms and conditions of the stock contract among the stockholders and between the stockholders and Reading Company, in view of the absence thereof in the charter, as heretofore pointed out.

The Questions Involved.

Under the decree of the District Court (Transcript, p. 287), which made mandatory the segregation plan as modified (Transcript, p. 274), the Reading Company is required to sell, assign and transfer, subject to the lien of the General Mortgage, all its right, title and interest in and to the stock of the Coal Company to a new corporation, in consideration of the payment by the new corporation to Reading Company of the sum of $5,600,000 and the agreement of the new corporation to issue its 1,400,000 shares of stock, without par value, to the stockholders of the Reading Company, preferred and common, share and share alike, for $5,600,000, or $2 for each share of Reading stock (Transcript, p. 275), and, in addition thereto, the Coal Company will pay to Reading Company $10,000,000 in cash, or current assets at market value, and $25,000,000 in new 4% Mortgage bonds of the Coal Company; and Reading Company will agree with the Coal Company that, at or before the maturity of the General Mortgage bonds, it will obtain the release of the Coal Company's property from the lien of the General Mortgage and discharge the Coal Company from liability on the General Mortgage bonds (Transcript, pp. 274, 275).

In other words, Reading Company will receive in the aggregate $40,600,000 for its entire interest in the Coal Company (Transcript, p. 163).

The interest of Reading Company in the Coal Company, as shown by its balance sheet as of December 31,

1919 (Transcript, pp. 114, 115), was carried on its books as follows:

The Philadelphia and Reading Coal and Iron Company's stock.....	$8,000,000.00
The Philadelphia and Reading Coal and Iron Co.	69,919,770.06
Total	$77,919,770.06

The same balance sheet shows that on December 31, 1919, the profit and loss account, or corporate surplus, of Reading Company was $33,201,149.81 (Transcript, p. 115).*

From the foregoing, it will be seen that upon the disposition of its interest in the Coal Company, Reading Company will receive assets to the amount of $40,600,000 and will surrender assets of a book value of $77,919,770.06, leaving a deficiency of $37,319,770.06, and this deficiency will more than wipe out the corporate surplus of upwards of $33,000,000.

Reading Company in its answer to intervening petitions and cross petition (Transcript, p. 153) admits that this will be the effect of the consummation of the Plan as modified and made mandatory by the decree appealed from, but explains that this effect will be more than counterbalanced by the taking up on the books of Reading Company the corporate surplus of the Railway Company, with which Reading Company is to be merged or consolidated, to the end that the final corporate surplus will exceed the existing corporate surplus of upwards of $33,000,000 (Transcript, p. 169), as illustrated by the balance sheets annexed as an exhibit to said answer and cross petition (Transcript, p. 200), wherein it is shown

* The balance sheet of Reading Company as of December 31, 1920 (Transcript, p. 200), has not been used because it does not separately show the Coal Company's stock, but the items appearing thereon for the indebtedness of the Coal Company to the Reading Company and the corporate surplus of the Reading Company are substantially the same as those given above for December 31, 1919.

that the corporate surplus of $33,996,983.01 as of December 31, 1920, will be $54,115,478.43 after the merger or consolidation of the Reading Company and the Railway Company.

The first and second preferred stocks of Reading Company are "entitled to non-cumulative dividends at the rate of, but not exceeding, four per cent. per annum, in each and every fiscal year, in preference and priority to any payment in or for such fiscal year of any dividend on" the common stock (Transcript, pp. 88, 90), and full dividends, at the rate of 4 per cent. per annum, on both the first and second preferred stocks, have been paid since the year 1903 (Transcript, pp. 103, 104).

These appellants contend, therefore, that, inasmuch as the preferred stocks have received their full dividends and the disposition of the interest of Reading Company in the Coal Company results in a depletion of the corporate surplus,* the preferred stocks are not entitled to share in such disposition.

These appellants further contend that, inasmuch as Reading Company owns all of the stock of the Railway Company, and may, therefore, at any time transfer the corporate surplus of the Railway Company to itself, it is no answer to say that the depletion of the corporate surplus of Reading Company may be made good by the surplus of the Railway Company. For all practical purposes, the two surpluses are merely parts of the same surplus.

Some suggestion has been made to the effect that the debt of the Coal Company to Reading Company, which on December 31, 1919, was $69,919,770.06 (Transcript, p. 114) and on December 31, 1920, was $69,357,017.99 (Transcript, p. 200), as above pointed out, is not real.

*A depletion of the corporate surplus is not necessarily the *natural* result of disposing of this interest under the mandate of this Court, but it is necessarily the result of the *artificial* features of the plan, as hereinafter set forth.

This debt was discussed by Circuit Judge McPherson in the earlier proceedings in the District Court, where, among other things, the Court found that

> "the debt is certainly carried on the books of both companies as an open account between them, and instalments of interest are certainly being paid thereon from time to time."
>
> (226 Fed. Rep. 229, at p. 269.)

This item of debt has not remained constant, but has varied from time to time since December 1, 1896, and interest thereon, in varying amounts, was paid, or credited, by the Coal Company to the Reading Company during each of the years 1900 to 1913, inclusive (Transcript, pp. 105, 106).

But it is not material for the purposes of this discussion whether the item is a genuine debt or not. The Reading Company carries it as an asset (Transcript, p. 114), and the Coal Company carries it as a liability (Transcript, p. 116). If it should be wiped out, the result would simply be to increase by that amount the value of the Coal Company's stock, all of which is owned by the Reading Company. The principles here involved will not, therefore, be affected by any discussion of the genuineness of this item, and the appellee Reading Company concurs in this view (Transcript, p. 162).

The position of these appellants is that, at least so long as the Reading Company continues to exist and function, all of its surplus, being an amount equal to the difference between the value of the assets, on the one side, and debts and par amounts of capital stock, on the other side, belongs to the common stockholders after "non-cumulative dividends at the rate of, but not exceeding, four per cent. per annum, in each and every fiscal year" shall have been paid to the preferred stocks.

The position of these appellants is, further, that assets of a corporation may be distributed to its stockholders

in only two ways: first, either in cash or property by way of dividends, where there is a surplus against which the distribution may be charged, and, second, by way of distribution of capital which necessitates reduction of the capital stock, it being apparent that any distribution of assets to the stockholders must result either in depleting the surplus or reducing the capital stock.

In view of this position, these appellants have contended, and now contend, that the disposition of the interest of Reading Company in the Coal Company provided in the Plan as modified and as made mandatory by the decree of the District Court confers upon the preferred stockholders a benefit to the prejudice of the legal rights of the common stockholders.

In order to bring this Plan into harmony with the legal rights of the common stockholders, these appellants made three suggestions to the District Court, which were to treat the disposition of the interest of Reading Company in the Coal Company as either

> (1) A distribution of capital, in which case the capital stock, preferred and common alike, should be reduced by the amount of such distribution; or
>
> (2) A distribution of surplus, in which case it should be made to the common stock alone; or
>
> (3) A sale of assets, in which case the proceeds should be placed in the treasury of Reading Company.

The first and third suggestions avoided the necessity of deciding the question as to the respective rights of the preferred and common stocks in the surplus of the Company, or of deciding what are the rights of the preferred stock therein. The second suggestion was based upon the assumption that the decision, if it were made, would

be in favor of the common stockholders—that is, that they own the surplus.

All of these suggestions were disregarded and this appeal is the result.

Specification of the Errors.

1. The Court erred in approving that part of paragraph 5 of the Modified Plan as supplemented by the provisions of sub-paragraph (*c*) of paragraph 3 of said decree which provides that the Reading Company shall offer for subscription to its stockholders, preferred and common, share and share alike, at $2. for each share of Reading stock, assignable certificates of interest in the stock of the new corporation to which the Reading Company shall, subject to the lien of the General Mortgage, sell, assign and transfer all its right, title and interest in and to the stock of Philadelphia & Reading Coal & Iron Company (hereinafter called the "Coal Company").

2. The Court erred in ordering the consummation of the provisions of that part of paragraph 5 of the Modified Plan as supplemented by the provisions of sub-paragraph (*c*) of paragraph 3 of said decree which provides that the Reading Company shall offer for subscription to its stockholders, preferred and common, share and share alike, at $2 for each share of Reading stock, assignable certificates of interest in the stock of the new corporation to which the Reading Company shall, subject to the lien of the General Mortgage, sell, assign and transfer all its right, title and interest in and to the stock of the Coal Company.

3. The Court erred in holding that the disposition of the right, title and interest of the Reading Company in and to the stock of the Coal Company provided for in paragraph 5 of the Modified Plan as supplemented by the

provisions of said decree does not confer upon the holders of the preferred stock of the Reading Company a benefit to the prejudice of the legal rights of the holders of the common stock of the Reading Company.

4. The Court erred in holding that the disposition of the right, title and interest of the Reading Company in and to the stock of the Coal Company as set forth in paragraph 5 of the Modified Plan as supplemented by the provisions of said decree is a sale to the stockholders of the Reading Company of such right, title and interest.

5. The Court erred in holding that the sum of $5,600,000, or $2.00 for each share of stock of the Reading Company, is an adequate consideration for the disposition of the right, title and interest of the Reading Company in and to the stock of the Coal Company.

6. The Court erred in holding that the disposition of the right, title and interest of the Reading Company in and to the stock of the Coal Company as set forth in paragraph 5 of the Modified Plan as supplemented by the provisions of said decree is a disposition of a part of the capital of the Reading Company.

7. The Court erred in not holding that the disposition of the right, title and interest of the Reading Company in and to the stock of the Coal Company as set forth in paragraph 5 of the Modified Plan as supplemented by the provisions of said decree effectuates a distribution in part at least of or from the surplus net profits of the Reading Company.

8. The Court erred in holding that it was warranted in treating as acquiescing in the Modified Plan the holders of common stock of the Reading Company who had failed to object thereto.

9. The Court erred in holding that it was justified in concluding from the positive attitude of a holder of 100,000 shares of common stock of the Reading Company that the remainder of the holders of such stock who failed to object to the Modified Plan were not only passively acquiescing in, but really actively approving, the same.

10. The Court erred in that it did not hold that the disposition of the right, title and interest of the Reading Company in and to the stock of the Coal Company provided in paragraph 5 of the Modified Plan as supplemented by the provisions of said decree is in violation of the legal rights of the holders of the common stock of the Reading Company.

11. The Court erred in that it did not hold that the holders of the common stock are solely entitled to distributions out of surplus net profits of the Reading Company of years other than those in which the full dividends shall not have been paid on the first and second preferred stock.

12. The Court erred in that it did not hold that the disposition of the right, title and interest of the Reading Company in and to the stock of the Coal Company as set forth in paragraph 5 of the Modified Plan as supplemented by the provisions of said decree is not a sale of such right, title and interest.

13. The Court erred in that it did not hold that the disposition of the right, title and interest of the Reading Company in and to the stock of the Coal Company as set forth in paragraph 5 of the Modified Plan as supplemented by the provisions of said decree is a distribution in part at least of or from the surplus net profits of the Reading Company.

14. The Court erred in that it did not hold that the holders of the preferred stock of the Reading Company are entitled to non-cumulative dividends not exceeding 4% per annum and no more.

15. The Court erred in that it did not hold that the Modified Plan as supplemented by the provisions of said decree does not effectuate a dissolution or liquidation of the Reading Company.

16. The Court erred in holding that the right of the stockholders of the Reading Company to participate in the disposition of the right, title and interest of the Reading Company in and to the stock of the Coal Company is based on the corporate right of all shareholders in a Pennsylvania Corporation to share equally on a disposition of its assets.

17. The Court erred in not holding that the rights of the stockholders of the Reading Company to participate in the disposition of the right, title and interest of the Reading Company in and to the stock of the Coal Company are determined by the contractual rights existing between the Reading Company and its stockholders and among said stockholders, which contractual rights are expressed in the certificates of the first preferred, second preferred and common stocks of the Reading Company.

ARGUMENT.

I.

The disposition of the interest of Reading Company in the Coal Company required by the decree is not a sale.

The disposition of the interest of Reading Company provided for in the Plan as modified and as made mandatory by the decree appealed from is not a sale in any real sense.

It is true that this disposition takes the technical form of a sale, in that title to property is to pass in consideration of the payment of a price, but all resemblance to a real sale ends there.

The price is purely arbitrary, and the Plan as modified and made mandatory by the decree contains no intimation, much less explanation, of how this price was determined. The appellee Reading Company, in its answer to intervening petitions and cross petition, states:

> "It is evidently impracticable to ascertain the market value of the coal stock * * * without offering it for sale. An appraisal would be of no use whatever under the circumstances. The Reading Company is under the necessity of making an actual disposition of the stock and no theoretical valuation of appraisers or experts could be of the least service unless they were willing and able to back the appraisal with a bid" (Transcript, p. 163).

It is suggested, however, that a valuation of appraisers or experts, no matter how theoretical, would be entitled to more serious consideration than a purely arbitrary and wholly unexplained price.

This answer and cross petition also states:

> "The coal stock is being sold for less than its book value and it is not asserted on behalf of the intervening common stockholders that it can be sold for as much as its book value. The sale results in a loss on the books of the Reading Company, yet the intervening common stockholders ask that it be treated as a distribution of profits and that the preferred stockholders be excluded from participation in the purchase on that theory" (Transcript, pp. 163, 164).

While these appellants do not assert that said stock can be sold for as much as its book value, they do assert that it can be sold for a price far in excess of the price named in the Plan as modified and made mandatory by the decree. This assertion is not based upon any theoretical valuation of appraisers or experts, but upon actual market conditions. In the affidavit of Austin W. Penchoen, verified March 12, 1921, and contained in the petition of Frances T. Ingraham *et al.*, it is stated:

> "That since the Reading plan was announced, the sale for the rights for each share of the Reading stock has been as follows:
>
> High 20
> Low ..... 13½"
> (Transcript, p. 128.)

The Reading plan referred to in the foregoing quotation is the plan which was filed in the District Court on February 14, 1920 (Transcript, p. 40), and the foregoing quotation means that between that date and March 12, 1921, holders of stock of Reading Company were able to sell their rights to participate in the disposition of the interest of the Reading Company in the Coal Company at from $13.50 to $20 per share of Reading Company stock, whereas the Plan as modified and made mandatory by the decree entitles them to said rights upon the payment of $2 per share of Reading Company stock.

These high and low prices reflect the public opinion of the value of the interest of Reading Company in the Coal Company during the period referred to, and, while they do not necessarily indicate the price at which this entire interest could have been sold, they are sufficient to show the purely arbitrary nature of the price named in the Plan as modified and made mandatory by the decree and of the gross inadequacy thereof.

That the sale results in a loss on the books of the Reading Company is due to the purely arbitrary and wholly unexplained price and the evident inadequacy of such price.

Nevertheless, said answer and cross-petition states that

> "The sale is compulsory and will result in a loss, not a profit" (Transcript, p. 162).

and that

> "It is the nature of the asset disposed of, and the method of its disposition, not the effect of such disposition on the books of the corporation, which fixes the rights of stockholders in respect of such disposition" (Transcript, p. 165).

That the sale is compulsory is due to the mandate of this Court, but that the sale will result in a loss and not a profit, is due to the price that has been fixed by Reading Company in its uncontrolled discretion. And, granting, for purposes of argument, that it is the nature of the asset disposed of, and the method of its disposition, not the effect of such disposition on the books of the corporation, which fixes the rights of the stockholders in respect of such disposition, this cannot be true where the method of disposition is to distribute assets of a corporation to its stockholders, preferred and common, share and share alike, under the guise of a sale and at a purely nominal price, and thus arbitrarily produce an effect on the books of the corporation which adversely affects the rights of the common stockholders in respect of such disposition.

The loss on the books of the Reading Company that results from this sale, and that these appellants are asking to be treated as a distribution of profits, is represented, in part at least, by the difference between the arbitrary and unexplained sale price and the real value of the interest that is being disposed of, and, under the Plan as modified and made mandatory by the decree, the preferred stockholders would benefit to the extent of one-half of that difference. In other words, this loss is a purely artificial one that has been created by means of the arbitrary and unexplained sale price, and apparently for the purpose of permitting the preferred stockholders to reap the benefit to which these appellants claim the preferred stockholders are not entitled.

II.

The so-called sale of the interest of Reading Company in the Coal Company required by the decree is not in conformity with previous decrees of the Federal Courts under similar circumstances, particularly the Union Pacific-Southern Pacific segregation, so far as the relative rights of the common and preferred stocks are concerned.

The Plan as modified (Transcript, p. 274) and made mandatory by the decree recites that

> "It is proposed to carry out this sale in accordance with the precedent established by the Union Pacific-Southern Pacific case, by issuing to Reading stockholders, with or without the intervention of a

trustee, as may be provided for in the final decree of the Court, assignable certificates of interest in the stock of the new corporation exchangeable for such stock only when accompanied by an affidavit that the holder is not the owner of any stock of the Reading Company" (Transcript, pp. 275, 276).

In the petition of the appellants Adrian Iselin *et al.*, representing holders of the first and second preferred stock of Reading Company, it is stated that the proposed distribution is in conformity with previous decrees of the Federal courts under similar circumstances, and the decree in the *Union Pacific-Southern Pacific* case is given as an illustration (Transcript, pp. 137, 138). This alleged similarity between the Plan as modified and made mandatory by the decree and the plan carried out in the *Union Pacific-Southern Pacific case,* so far as it relates to the treatment of the relative rights of the common and preferred stocks, will not bear analysis. As is hereafter shown, the treatment accorded by the Union Pacific Railroad Company to its common stockholders is precisely the treatment that these appellants contend should be accorded by the Reading Company to its common stockholders.

In that case, after the decision of the Supreme Court and before the mandate therein had issued, the Government and the Union Pacific and the Oregon Short Line united in a motion to this Court praying for advice to the District Court as to the form of the mandate.

It will be recalled that the stock of the Southern Pacific Company, which this Court ordered the Union Pacific and Oregon Short Line to dispose of, belonged not to the Union Pacific, but to the Oregon Short Line, the stock of which was owned by the Union Pacific. It was analogous to the surplus of the Reading Railway Company in this case. In the *Union Pacific* case, therefore, the situation being dealt with was analogous to the

situation being dealt with in this case as to the Reading Railway Company's surplus and one step further removed than the Reading Company's surplus of $33,000,000, which also is involved in this case.

In their said joint motion to this Court, the Government and the railroad companies joined in asking the Court:

> "to instruct the United States District Court for the District of Utah, by a provision incorporated in the mandate of this court, when issued, or otherwise, whether or not a sale of the Southern Pacific Company shares held by said appellees to the shareholders of appellee Union Pacific Railroad Company, substantially in proportion to their respective holdings, *or a distribution thereof by dividend to the Union Pacific stockholders entitled to such dividend,* would, in the opinion of this court, constitute a disposition of said shares in compliance with the opinion herein filed on December 2, 1912." (Italics are ours.)
>
> *U. S.* v. *Union Pacific R. R. Co.*, 226 U. S., at p. 471.

Also counsel for the Union Pacific and Oregon Short Line, in their printed argument to the Supreme Court on said motion, used the following language:

> "While no plan for the disposition of said Southern Pacific Company shares has been definitely matured, it is considered for reasons hereinafter stated that the only practicable method for the disposition of said shares without irreparable injury would be for the Union Pacific Railroad Company to offer said shares to its own shareholders *pro rata* according to the amount of their holdings, for purchase *at a fair price or to distribute the same as a dividend to the holders of its stock entitled to such dividend.*" (Italics are ours.)

The Union Pacific and its counsel were always alive to and observant of the respective rights of their preferred

and common stocks. Manifestly they never entertained any thought that the preferred stockholders were entitled to a dividend above their 4%. They submitted to the Court the alternatives of purchase *at a fair price* or distribution by dividend to the *stockholders entitled to such dividend.* That was in September, 1913. In January, 1914, when the Company came to the point of declaring the extraordinary dividend of $80,000,000 (largely out of the proceeds of the sale), that was challenged by the preferred stockholders and resolved against them (*Equitable Life Assurance Society* v. *U. P. R. R. Co.*, 212 N. Y. 360), all of that dividend was declared to the common stock and was sustained.

This Court in the Union Pacific dissolution accepted the alternative of *sale* to all the stockholders, both common and preferred, but it was a very real sale. The decree provided that the offering should be at such price and upon such other terms as the defendants, Union Pacific Railroad Company and Oregon Short Line Railroad Company, should determine (*Section 5 of decree of June 30, 1913. Decrees and Judgments in Federal Anti-Trust Cases published by Government Printing Office, 1918, page 221*). The price so fixed was $92 per share (which included about $4 of accumulated dividends).

The high and low prices on the New York Stock Exchange for Southern Pacific Company's stock in the years 1911, 1912 and 1913 were respectively:

	High.	Low.
1911	126⅜	104½
1912	115½	103½
1913	110	83

The low price in June, 1913 (the date of the decree) was 89⅜, and it never sold on the market above 90⅝ during the rest of that year (*The Financial Review, New York, 1914, pages 139, 142, 145*). What was done in the Union Pacific case was a *sale, not a distribution,* but in

the instant case, while the plan calls it a sale, the price to be paid is only $2 per share of Reading stock (producing $5,600,000), which works out to a payment for the present Coal Company's stock of $35 per share ($8,000,000 of stock of $50 per share is 160,000 shares, which at $35 per share produces $5,600,000), whereas the book value of the Coal Company's stock after this transaction has been consummated and the $35,000,000 cash and bonds have been paid out and issued, making the surplus of the Coal Company $60,000,000, will be about $425 per share, as hereinafter explained.

And so the real result of the so-called sale in the instant case is not a sale for anything approaching the value of the assets sold, but is a price less than one-tenth of the real value, the rest being made up, however the figures may be turned and twisted, by the absorption of the surplus of the Reading Company, that is, the distribution to the Reading preferred and common stockholders alike, of the surplus of the Reading Company.

The *Union Pacific-Southern Pacific* case, therefore, instead of being a precedent to support the present transaction, is a precedent exactly opposite, because in that case the company contemplated and offered to the Court the alternatives of a real sale to all of the stockholders or a dividend to the stockholders entitled to a dividend, and the Court having accepted the former alternative, the company carried out the plan by a sale at a price approximating the then market value of the stock.

In this case the Reading Company contemplated and offered to the Court no alternative whatever, but was successful in having the Court accept and make mandatory a Plan providing for the disposition of its assets at a price which is arbitrary, wholly unexplained and manifestly inadequate.

If Reading Company had followed in the footsteps of the Union Pacific Railroad Company and had obtained

the sanction of the District Court to such a plan as was consummated by the Union Pacific Railroad Company, these appellants would not be before this Court with this appeal. In fact, as is more fully set forth under III hereof, these appellants suggested to the District Court a modification of the Reading plan that would have been satisfactory to them and that would have obviated this appeal, which suggestion was to the effect that the interest of Reading Company in the Coal Company should be sold at as nearly as possible its market price, and that the proceeds of the sale should be placed in the treasury of Reading Company, precisely as was done by Union Pacific Railroad Company in the disposition of its interest in the Southern Pacific Company.

Obviously, it is idle for Reading Company and the representatives of the holders of its preferred stock to cite as a precedent for the plan of which these appellees are complaining a plan substantially similar to modifications of the Reading plan that were suggested by these appellants in the District Court.

III.

If the disposition of the interest of Reading Company in the Coal Company required by the decree is intended to be a sale, the decree should be so modified as to carry out such intent.

It has already been shown that the disposition by the Reading Company of its interest in the Coal Company as required by the decree is not a sale in any real sense, and that it is the disposition of such interest at an arbitrary, wholly unexplained and manifestly inadequate

price and the resulting depletion of the corporate surplus of Reading Company that has brought on the controversy out of which this appeal arises.

In order to avoid the necessity either of ascertaining the true value of such interest or of determining the respective rights of the preferred and common stocks therein, these appellants suggested to the District Court at the hearing on May 2, 1921, and now suggest to this Court, the following modification of the plan made mandatory by the decree:

> Certificates of the interest of the Reading Company in the stock of the Coal Company, such interest being the equity over and above the lien of the General Mortgage referred to in said Plan, shall be dealt with as follows:
>
> A. The certificates of interest shall be lodged with a trustee to be appointed by the District Court, or shall be transferred to a new corporation to be made a party to the proceeding below and subjected to the control of the District Court.
>
> B. Such trustee or new corporation shall, under the control and direction of the Court, exercise the voting power of the Coal Company stock and receive the dividends thereon pending the sale of the certificates of interest.
>
> C. Reading Company shall proceed to sell the certificates of interest to such purchasers and under such restrictions as may be approved by the District Court, to the end that the purposes of the mandate of this Court may be fully effectuated and within such time as the District Court may grant for the purpose of accomplishing such sale to the best advantage.
>
> D. If desirable and practicable, the Coal Company may be consolidated with Delaware Coal Company, of which it owns the entire capital stock, and the consolidated company may then issue 1,400,000 shares of stock, without par value. These

shares shall be placed under the lien of the General Mortgage in lieu of the present Coal Company stock, and be dealt with as provided above. If such consolidation is not practicable, the new corporation suggested in paragraph "A" may issue 1,400,000 shares of stock, without par value, to be sold as provided in paragraph "C".

This suggestion contemplates that no distribution whatever be made to the stockholders of Reading Company, and that the proceeds of the sale of its interest in the Coal Company be placed in the treasury of Reading Company, to be dealt with as any other treasury assets.

This suggestion is based upon the plan recently approved by the Government and adopted by the Supreme Court of the District of Columbia in the case wherein the Armour and Swift packing companies were required to dissolve their relations with numerous stockyard companies by disposing of their stock holdings therein. It is analogous to the method employed in the *Union Pacific-Southern Pacific* case, wherein the Union Pacific Railroad Company sold its interest in the Southern Pacific Company at approximately the market price and placed the proceeds of the sale in its treasury.

This suggestion, by keeping the voting power of the Coal Company's stock and the right to receive the dividends thereon under the control of the District Court until such time as the interest of the Reading Company therein can be sold to purchasers who are independent of the Reading Company, insures compliance with the mandate of this Court. By allowing such time as to the District Court may seem proper within which to sell the interest of Reading Company in the Coal Company stock, and by permitting the Reading Company to manage its sale, a sacrifice of the same in a market overhung by abnormal financial conditions is made unnecessary. And by reason of the fact that the proceeds of such sale would

go into the treasury of the Reading Company, and be dealt with as any other treasury assets, this suggestion makes unnecessary any discussion of the respective rights of the preferred and common stocks, because it does not, as does the Plan made mandatory by the decree, raise any questions regarding such rights.

IV.

The disposition of the interest of Reading Company in the Coal Company under the decree cannot be justified on the ground that it is a disposition of a capital asset.

The answer to intervening petitions and cross petition of the appellee Reading Company (Transcript, p. 153) attempts to justify the distribution of the interest of Reading Company in the Coal Company to the stockholders, preferred and common, share and share alike, on the ground that it is a disposition of a capital asset.

This attempt, as we understand it, is supported on the theory that certain assets are earmarked as capital assets, and have some characteristics that distinguish them from other assets of the corporation.

This theory seems to arise from the mistaken assumption that only such assets as have come to the corporation as earnings, income or profits may be distributed to stockholders by way of dividends, and that the distribution of an asset that was acquired by a corporation out of capital originally subscribed by its stockholders takes on some characteristics that distinguish it from an ordinary dividend and that preclude its being dealt with as such.

As illustrating this, let it be assumed that a corporation commences business with a capital of $100,000 in

cash paid in by its stockholders; that, out of such cash, it expends $50,000 in the purchase of securities for permanent investment; that thereafter it expends, out of the cash derived from earnings, income and profits, a further sum of $50,000 for the acquisition of additional securities for permanent investment. If thereupon the corporation should declare a dividend of $50,000, to be paid by a distribution of the securities first acquired, could it be said that such distribution would not be governed by the ordinary rules of law relating to dividends, but would be governed solely by the fact that it was a distribution of "capital assets", and, therefore, taken out of the rules of law relating to dividend distributions, in case any contest between the preferred and common stockholders should arise in respect thereto? The assumption of the appellee Reading Company, as applied to this case, would require that the securities first acquired and out of capital could not be distributed as a dividend, and that only the securities later acquired and out of earnings, income and profits could be so distributed.

But a corporation in dealing with its assets is not required to classify its assets as between those that were acquired by means of the contributions of its stockholders to its capital and those that are acquired from time to time through earnings, income and profits. Nor is it required to make distributions of its assets to its stockholders according to such classification and practically in specie, as the foregoing assumption suggests.

We are unable to discover any authority for the theory that is advanced or the assumption from which it seems to arise. The authorities are to the contrary, and sustain the following propositions:

1. That the surplus of a corporation is the difference between the value of its assets, on the one side, and the debts and par amounts of capital, on the other side.

2. That none of the assets of a corporation is identified as capital, and none is identified as surplus.

3. That, where a surplus exists, it may be distributed to the stockholders entitled thereto, either in money or in property.

The Supreme Court of Iowa, in *Hubbard* v. *Weare* (79 Ia. 678, at pp. 688-9; 44 N. W. Rep., at p. 918), states the rule as follows:

> "Some difference is expressed as to what are profits, and how they are to be arrived at. This is answered in *Miller* v. *Bradish*, 69 Iowa, 278 (28 N. W. Rep. 594), where it is said: 'The assets, resources, and funds of the corporation must consist of cash on hand and other property, and, if such assets exceed the liabilities, a dividend can lawfully be declared;' in other words, a profit exists."

The Court of Appeals of the State of New York, in *Williams* v. *Western Union Telegraph Co.*, 93 N. Y. 162, discussed at length the meaning of "capital stock" and "surplus", with citation of authorities. Earle, *J.*, lays down the rule that when a corporation's property exceeds the amount of capital stock limited by its charter, the excess is surplus.

> "Such surplus belongs to the corporation and is a portion of its property, and, in a general sense, may be regarded as a portion of its capital, but in a strictly legal sense it is not a portion of its capital, and is always regarded as surplus profits" (at p. 188).

And as to the distribution thereof the opinion continues:

> "The surplus may be in cash, and then it may be divided in cash; it may be in property, and if the property is so situated that a division thereof among

the stockholders is practicable, a dividend in property may be declared, and that may be distributed among the stockholders" (at p. 189).

The Appellate Division of the New York Supreme Court, First Department, in the case of *Russell* v. *American Gas & Electric Co.* (152 A. D., at p. 138), lays down the rule in the following language:

> "Where a corporation has property in excess of the amount of its capital stock, the excess is surplus which may be divided among the stockholders entitled to share therein, either in money or property."

In the recent case of *Anderson* v. *Farmers' Loan and Trust Co.,* decided by the United States Circuit Court of Appeals, Second Circuit (241 Fed. Rep. 322), the Court discusses the question as to whether any particular assets of a corporation can be identified as forming its capital or any particular assets can be identified as forming its surplus, and reaches the following conclusion:

> "The words 'capital, surplus and undivided profits' relate to no particular kind of property, but are expressions describing the amount of the residue of the assets after the liabilities have been deducted" (at pp. 326, 327).

And again on page 328:

> "We do not regard any specific assets as constituting capital of the company. The capital, and in the same way the surplus and undivided profits, are the residue left after paying the obligations of the bank to its depositors, and any other indebtedness it may have. These claims may be satisfied out of any property, and the balance remaining, which is the capital, surplus and undivided profits, is to be imputed equally to all kinds of property which the trust company may possess."

In that case the Court was considering the situation of a trust company which, by the New York statute, was

required to have a certain portion of its capital invested in certain kinds of securities. Therefore, the trust company contended that it could point to such securities and name them as a part of its capital; and the Court, after full discussion and citation of authorities, reached the conclusion that the rule is sound that these items, capital and surplus, applied to a corporation, are mere bookkeeping items, that they point to no particular investments, that they are merely the difference between the assets and liabilities of the corporation, and that, after deducting them from the amount of the capital stock, the balance is surplus.

This Court, in *St. John* v. *Erie Ry. Co.,* 22 Wall. 136, at page 149, states the legal principle as follows:

> "There is nothing in the agreement or the statute, and we are aware of no legal principle which would authorize the stockholders in question to analyze the business, select out a part of it, and to say that the *net earnings* specified must be a predicate of that part, and of none other. The Company had the right to conduct its operations, in good faith, as it might see fit; and it was from them and all of them that the materials for the computations of earnings were to be derived" (italics ours).

An exhaustive search of the authorities has failed to disclose any case where the respective rights of the preferred and common stockholders of a corporation in a distribution of its assets were held to be governed by the nature of the assets distributed, the time at which the assets were acquired or the manner in which they were acquired, whether out of the contributions of the stockholders to the capital of the corporation, or out of the earnings, income or profits.

Up to the point of encroaching on the capital, it is immaterial how the distribution is made. It is a dividend and it may be paid either in cash or in property.

V.

If the disposition of the interest of Reading Company in the Coal Company required by the decree is intended to be a distribution of capital, the decree should be so modified as to carry out such intent.

It is obvious that the assets of a corporation may be distributed to its stockholders in only two ways: first, either in cash or property by way of dividends, where there is a surplus against which the distribution may be charged, and, second, by way of distribution of capital, which necessitates a reduction of the capital stock.

Having suggested that if the disposition of the interest of Reading Company in the Coal Company required by the decree is intended as a sale, the decree should be so modified as to carry out such intent, and having suggested a modification of the Plan as made mandatory by the decree for the purpose of carrying out such intent, these appellants further suggest that if the disposition of the interest of Reading Company in the Coal Company is intended to be a distribution of capital, the decree should be so modified as to carry out that intent.

These appellants suggested to the Court below, and now suggest to this Court, a modification of the Plan approved and made mandatory by the decree which will bring the Plan and decree into harmony with the contention of the appellee Reading Company that it brings about a distribution of capital. This suggestion is set forth in the petition of these appellants for leave to intervene (Transcript, p. 96), and is set forth and more fully explained in their amended and supplemental petition for modification of the plan of dissolution (Transcript, p. 101), and is as follows:

> "XIII. That inasmuch as the Reading Company is obliged under the decree of the Court to divest

itself of said assets, being the stock and debt of defendant Coal & Iron Company, and under said plan receives therefor considerations which fall short of the value of said assets, it appears to be necessary either (*a*) to eliminate the surplus of defendant Reading Company as it now exists or to reduce the surplus of the Reading Company as it will exist after the proposed merger with the Philadelphia & Reading Railway Company, or (*b*) to reduce the capital stock of the Reading Company, provided that the principle of said plan is to be carried out of making an equal distribution to both the preferred and common stocks in connection with the divesting of said assets. That in order to obviate such inequity arising under said plan, your petitioners respectfully suggest the following modification thereof by the addition to article 5 thereof of the following:

'Coincidently with the issuance and distribution of the certificates of interest in the Coal Company stock, as aforesaid, the Reading Company will reduce its capital stock by the amount of $..... such reduction to apply to all shares of the stock of the Reading Company equally, regardless of classification into preferred and common, and such reduction to be effected by decree of the Court directing it should the Court accept this plan and so decree.

'For the purposes of carrying out such a provision, jurisdiction of the case shall be retained by the Court.'

"That the amount by which such reduction should be made is the net value of the assets of which the Company is required to divest itself, namely:

"The true value of the $8,000,000 capital stock of the Coal Company and of the $69,919,770 debt of the Coal Company to the Reading Company, such value to be ascertained in such manner as to this Court shall seem proper and sufficient, less $25,000,000 bonds and $10,000,000 cash or current assets to be received from the Coal Company and $5,600,000 cash to be received from the stockholders" (Transcript, pp. 109, 110).

This modification would bring about a true distribution of capital, and leave the surplus of Reading Company, whether disclosed or latent, untouched. Because of the fact that Reading Company has the right to redeem the preferred stock, a distribution of capital equally to all classes of stock amounts to a redemption of the preferred stock *pro tanto,* and, therefore, preserves all of the equities between all classes of stockholders.

The reason why, under this suggested modification, an appraisal of the value of the Coal Company's stock would be necessary is because that stock is worth much more than par, and so a distribution thereof to all stockholders by a uniform reduction of the capital stock, which, because of the redemption right against the preferred stocks would amount to a *pro tanto* redemption thereof, would not be equitable to the common stock if the Coal properties should be distributed on a valuation basis materially below their actual value. This may be illustrated by the fact that the Coal Company on December 31, 1920, had a surplus of over $25,000,000; that under the Plan as made mandatory by the decree, a debt of approximately $70,000,000 disappears, and new liabilities of $35,000,000 arise, or a net gain in the balance sheet of the Coal Company of $35,000,000; and that this added to the surplus, gives the Coal Company a surplus of $60,000,000, and makes the $8,000,000 of Coal Company stock worth, therefore, between eight and nine times its par value.

VI.

The disposition of the interest of Reading Company in the Coal Company under the decree cannot be justified on the ground that it is a partial liquidation of Reading Company.

The mandate of this Court pursuant to which the Plan made mandatory by the decree was evolved requires a dissolution of the relations between the Coal Company and the Railway Company that were maintained through the Reading Company's ownership of the entire capital stock of both companies, and thus requires a reorganization of the Reading Company's property holdings. In view of this, the suit brought by the Government in which the mandate was made is often loosely referred to as the "Reading Dissolution Suit" and the "Reading Reorganization Proceeding". Likewise the Plan is often loosely referred to as the "Reading Dissolution Plan" and the "Reading Reorganization Plan".

The only dissolution that is involved in this Plan, however, is the dissolution of the relation between the Coal Company and the Railway Company that was maintained through the Reading Company, and the only reorganization that is involved in this Plan is a reorganization of the property holdings of the Reading Company.

But the currency of these expressions seems to have suggested the theory that the disposition of the interest of Reading Company in the Coal Company required by the decree involves a partial dissolution and partial liquidation of the corporation. Consequently, there appears in the answer and cross petition of defendant Reading Company a discussion of "property of all the stockholders, preferred and common, share and share alike, available for equal distribution among them either upon dis-

solution of the company or its final or partial liquidation" (Transcript, p. 177).

But neither the mandate of this Court nor the Plan made mandatory by the decree involves any dissolution or reorganization of Reading Company, either in whole or in part, in a corporate sense. Reading Company was incorporated with a broad charter which places no limit upon its corporate activities, beyond providing that nothing therein contained "shall be so construed as to give to the said corporation any banking privileges or franchises, or the privileges of issuing their obligations as money" (Transcript, p. 191).

In said charter Reading Company is specifically given the power "to make purchases and sales of or investments in the bonds and securities of other companies" and "to receive and hold * * * any estate or property, real or personal * * * and also to pledge, sell and dispose thereof, on such terms as may be agreed on between them and the parties contracting with them" (Transcript, p. 192, sec. 3).

Acting under these powers, Reading Company in 1896 acquired all of the capital stock of the Coal Company and all of the capital stock of the Railway Company; and this Court having declared the ownership of such stocks by Reading Company to be unlawful, and having required Reading Company to dispose of the stock of the Coal Company, the Plan for such disposition need go no further than to require a sale of the interest of Reading Company in the Coal Company and the substitution of the proceeds of such sale for such interest in the Coal Company among the Reading Company's assets.

Such a plan would involve no corporate change in Reading Company, and such a sale is one that Reading Company could voluntarily make under its broad charter without violating its contract with its stockholders. Under such a plan, there would be no liquidation at all, partial or otherwise, but merely a substitution of one

asset for another; and any legitimate loss that might accrue from a *bona fide* sale, to the best advantage, of the interest of Reading Company in the Coal Company would be a proper charge to the surplus of Reading Company, and would meet with no objection on the part of its common stockholders.

But the Plan made mandatory by the decree places a purely arbitrary and wholly unexplained price upon the interest of Reading Company, which is clearly less than the value of such interest. Having thus artificially created a loss, the Plan proposes to charge this loss to surplus and to give the preferred stockholders equal rights with the common stockholders to participate in this so-called sale at an arbitrary and inadequate price. It is apparent that the preferred stockholders will be benefited by the difference between the value of their purchase and the price they pay for it, and it is also apparent that the loss that is involved in this sale will be made up out of surplus, and will, therefore, serve to reduce the same.

The effect of all this is precisely the same as if Reading Company should declare a dividend of the difference between the value of its interest in the Coal Company and the price for which such interest is to be sold under the Plan, distribute this dividend to all of its stockholders, preferred and common, share and share alike, and reduce the surplus by the amount of such dividend.

Naturally, the common stockholders object to this, on the ground that this distribution, which is a dividend in everything but form, is improper, by reason of the fact that the preferred shares are non-cumulative and that they have received all of the dividends to which they are entitled, and that the common stockholders are entitled to the surplus as against the preferred stockholders.

To meet this objection, the appellee Reading Company has undertaken to show that this distribution is

either a sale or is a disposition of a capital asset, or, finally, is a partial liquidation upon a partial dissolution of the company. For the reasons heretofore explained, these appellees contend that it is neither of these, but is, in substance, in effect, and in everything but form, a dividend, to which they are wholly entitled.

Any proceedings looking to a change in the structure or powers of a corporation must be taken pursuant to the laws of the State that gave the corporation its existence, and while the Federal courts, in the enforcement of provisions of the Sherman Act and the Interstate Commerce Act, may require corporations of the several States to change their business practices and to divest themselves of assets held by them in violation of such laws, the Federal courts do not undertake to bring about through their decrees changes in the structure of State corporations, and thus override the corporation laws of the several States.

In short, the Plan made mandatory by the decree does not involve a dissolution of Reading Company, either wholly or in part, nor does it involve a liquidation of its assets, either wholly or in part. It merely involves a substitution of one asset for another, in such a way, however, that a loss is artificially created and made up out of surplus, to the prejudice of the rights of the common stockholders.

VII.

The distribution of the interest of Reading Company in the Coal Company required by the decree effectuates a distribution, in part at least, of or from the surplus net profits of Reading Company.

Under the Plan as made mandatory by the decree, Reading Company will dispose of its interest in the Coal Company, which was carried on its books as of December 31, 1919, in the following items:

Coal Company's stock	$8,000,000.00
Coal Company's indebtedness to Reading Company	69,919,770.06
Total	$77,719,770.06

In respect of such disposition Reading Company will receive:

Cash, or current assets at market value, from the Coal Company	$10,000,000
Bonds of the Coal Company	25,000,000
Cash from the new corporation to which Reading Company will sell, assign and transfer, subject to the lien of the General Mortgage, all its right, title and interest in and to the stock of the Coal Company	5,600,000
Total	$40,600,000

This will result in a shrinkage in assets of the difference between these two totals, or, approximately, $38,000,000. As of December 31, 1919, the surplus of Reading Company was approximately $33,000,000 and the surplus of the Railway Company was approximately $44,000,000 (Transcript, pp. 115, 119). This shrinkage

in assets is to be made good in part by the Reading Company's surplus of $33,000,0000, which will thereby be absorbed and eliminated; but, as the Reading Company's surplus will not suffice by approximately $5,000,000 to make good this shrinkage in assets, this $5,000,000 deficiency is to be made up out of the surplus of the Railway Company, which, under the Plan, is to be consolidated with Reading Company. All of this is conceded by the appellee Reading Company, and is, in fact, illustrated by the tabulation of balance sheets (Transcript, p. 200) which accompanies its answer and cross petition, and which shows that as of December 31, 1920, the corporate surplus of Reading Company was approximately $34,000,000, and the corporate surplus of the Railway Company was approxiately $64,000,000—a total of $98,000,000—and that, after the consummation of the Plan and the consolidation of the Reading Company and the Railway Company, the corporate surplus of the consolidated corporation will be approximately $54,000,000.

The effect of this on the Reading Company's books is precisely the same as if it should declare a dividend of $38,000,000 and reduce its surplus by the amount of such dividend.

In an attempted justification of this result, the appellee Reading Company states in its answer and cross petition:

> "The capital of the Reading Company will remain unimpaired. Upon the consummation of the plan the assets of the Reading Company will exceed the aggregate of its capital stock and liabilities by an amount in excess of the present surplus of $33,000,000" (Transcript, pp. 165, 166),

and

> "The book surplus of the Reading Company will not be impaired. The book loss from the sale of

> the coal stock will be more than made up by taking up on the Reading Company's books in connection with the plan, the value of the railway property, as shown on the books of the Railway Company" (Transcript, p. 169),

which, as is further explained,

> "will more than counterbalance what it will be necessary to write off its investment in the Coal Company under the plan. So that in fact the surplus of the Reading Company, after the consummation of the plan, will be much greater than $33,000,000" (Transcript, p. 169).

This seems to proceed upon the theory that the common stockholders have no interest in the surplus of the Railway Company, and that, if the result of taking over the Railway Company's surplus on the Reading Company's books is more than to make good this shrinkage, and, therefore, leave on the Reading Company's books a surplus greater than the original surplus of $33,000,000, the common stockholders have no right to complain, and their rights have not been prejudiced.

This, of course, is no justification whatever. The Reading Company owns all of the capital stock of the Railway Company, and, therefore, owns all of the surplus of the Railway Company, which surplus it can reduce to possession either by causing the Railway Company to pay over the same as dividends, or by merging the Railway Company into itself, or consolidating with the Railway Company, as provided in the Plan. It follows that, if the Railway Company's surplus needs to be considered, it is merely necessary to add it to the Reading Company's surplus as carried on its own books, and to deal with the total as the surplus of the Reading Company, just as if the Reading Company had reduced the Railway Company's surplus to possession.

After the Coal Company has paid or delivered to the

Reading Company $10,000,000 in cash, or current assets at market value, and has delivered to the Reading Company $25,000,000 principal amount of its new 4% bonds, the interest of the Reading Company in the Coal Company is to be sold to a new corporation, in consideration of the sum of $5,600,000, and this new corporation is to issue 1,400,000 shares of stock and sell the same to stockholders of Reading Company, preferred and common, share and share alike, for $5,600,000, or $2 for each share of Reading stock (Plan as modified, par. 5; Transcript, p. 275).

In short, the interest of Reading Company in the Coal Company, through the medium of a new corporation, is to be distributed *pro rata* to its stockholders, preferred and common, share and share alike, upon payment by them of $2 for each of their shares in Reading Company, and, as the result of this, the corporate surplus of Reading Company is to be depleted to the extent of $38,000,000.

If the actual value of the interest of Reading Company in the Coal Company (after the delivery by the Coal Company to the Reading Company of $10,000,000 in cash or current assets and $25,000,000 in bonds) were no more than the $5,600,000 for which it is to be offered to the stockholders, preferred and common, share and share alike, the $38,000,000 would be a legitimate loss that could properly be charged against surplus of the Reading Company. On the other hand, none of the stockholders would receive any benefit whatever from such distribution, because the value of what they receive would be precisely what they pay for it. There would, therefore, be no controversy between the preferred stockholders and the common stockholders, and they would not be before this Court, the preferred stockholders supporting the Plan made mandatory by the decree and the common stockholders attacking it. It follows that, upon the payment of $2 per share of Reading stock for a *pro rata*

share of the interest of Reading Company in the Coal Company, each stockholder will receive something exceeding $2 in value, and it follows that the preferred stockholders are supporting the Plan for the purpose of reaping the benefit of such excess value.

The present value of the interest of Reading Company in the Coal Company may be less than the $78,000,000 at which it is carried on the Reading Company's books, but it is obviously more than the $5,600,000 for which it is to be sold to the stockholders; so that, while it may not be claimed that the distribution of the interest of the Reading Company in the Coal Company necessarily involves a distribution to its stockholders of the entire $38,000,000 by which its surplus is depleted, it does affect a distribution to its stockholders of so much of that $38,000,000 as represents the difference between the value of the interest to be distributed and the $5,600,000 that is to be paid therefor by its stockholders, and, there being $70,000,000 of first and second preferred stocks and $70,000,000 of common stock, it follows that the preferred stockholders will receive one-half of so much of the $38,000,000 as represents the difference between the value of the interest and the $5,600,000 that is to be paid therefor.

In its effect, therefore, upon the Reading Company and in its benefits to the stockholders, the disposition of the interest of the Reading Compaany in the Coal Company is precisely the same as if the Reading Company should pay to its stockholders, preferred and common, share and share alike, a dividend aggregating $38,000,000, less such part thereof, if any, as may represent the difference between the actual value of the interest of Reading Company in the Coal Company and the value of approximately $78,000,000 at which that interest is carried on the Reading Company's books. In other words, this disposition is a dividend, although it has been

given the appearance of a sale, and although the appellee Reading Company, in defense of the Plan made mandatory by the decree, has argued indiscriminately that it is a sale, that it is a distribution of a capital asset, and that it is a partial liquidation on partial dissolution, without taking any definite position as to which of the three it claims this distribution to be.

The means by which the Board of Directors of Reading Company have seen fit to bring about this effect cannot change its nature, and it is immaterial that they have given it the appearance of a sale and that they have not given it the name of a dividend. The courts are not influenced by these considerations, but look only to the substance.

In the *City of Allegheny* v. *Pittsburgh, A. & M. P. Ry. Co.,* discussed *infra,* the distribution by the defendant corporation to its stockholders of the entire capital stock of a controlled corporation was stated by the Pennsylvania Supreme Court to be the severance of the stock from the body of the corporate property; and yet it was held to be a dividend and taxable as such, although it was not called a dividend by the corporation.

In the cases of *United States* v. *Phellis, Rockefeller* v. *United States* and *New York Trust Co.* v. *Edwards,* Nos. 260, 535 and 536, respectively, October Term, 1921, and decided by this Court on November 21, 1921, the distributions to the stockholders represented the proceeds of the disposition of physical properties which the corporations had actually owned and operated. In the *Phellis* case the corporation had disposed of all of its assets and good will, and in the *Rockefeller* and *New York Trust Company* cases each of the corporations had disposed of the assets and good will connected with an important part of its business. The Reading Company has never owned and operated any physical properties, as had all of the corporations involved in the foreoging cases, and has

never engaged in the coal and railway business, as the Prairie Oil & Gas Company and the Ohio Oil Company, in the *Rockefeller* and *New York Trust Company* cases, had engaged in the oil and pipe line business. All that Reading Company has done since 1896 is to hold the entire capital stocks of a coal company and a railway company, the holding jointly of which has been declared by this Court to be unlawful and the acquisition of which was possible only by reason of the broad provisions of the charter of the Reading Company which gave it "the power to make purchases and sales of or investments in the bonds and securities of other companies". Nevertheless, in the foregoing cases this Court, after stating that each of the corporations had an excess of assets over liabilities showing a large surplus of accumulated profits, and after observing that the amount was not important, except that it was sufficient to cover the distributions to its stockholders that grew out of the disposition of the physical properties mentioned, declared the distributions to be dividends and taxable as income to the stockholders who received them.

VIII.

The holders of the preferred stock of Reading Company are entitled to non-cumulative dividends not exceeding four per cent. per annum, and no more.

As already explained, the contract among the stockholders and Reading Company is not set out, either in whole or in part, in the charter of the Reading Company, and must be found in the stock certificates (Transcript, pp. 88, 90, 92).

If there had been any previous negotiations, they would all be merged in the certificates, which must be taken to express the final intention (*Scott* v. *B. & O. R. Co.*, 93 Md. 475, at p. 498; 49 Atl. Rep. 327, at p. 328).

A. The Reading Company Stock Certificates.

The Reading Company stock certificates were not loosely drawn, but were prepared, as analysis discloses, with the greatest care, and with the intent not only to limit but to protect the preferred stocks in accordance with the understanding, and also to protect and limit the common stock.

The preferred stocks are

> "entitled to non-cumulative dividends at the rate of, but not exceeding, four per cent. per annum, in each and every fiscal year, in preference and priority to any payment in or for such fiscal year of any dividend on"

the common stock.

In order to make it doubly sure that the above limitation was effective, the certificate then used this language:

> "but only from undivided net profits of the company when and as determined by the Board of Directors, and only if and when the Board shall declare dividends therefrom."

The certificate of the first preferred stock provided that, at any time after dividends at the rate of four per cent. per annum should have been paid thereon for two successive years, the Reading Company might, without further consent from the holders or owners thereof, increase and issue first preferred stock to the extent of 420,000 shares for use towards the conversion of the second preferred stock; and the certificate of the second preferred stock provided that, at any time after dividends at the rate of four per cent. per annum should have been

paid for two successive years on the first preferred stock, the Reading Company, without further consent from the holder or owner of the second preferred stock, might exercise the right to convert the second preferred stock, not exceeding $42,000,000 at par, one-half into first preferred stock and one-half into common stock. Both certificates provided that the Reading Company should have the right at any time to redeem either or both classes of the preferred stock, at par in cash, if such redemption should then be allowed by law.

By conversion of the second preferred into half first preferred and half common, or by redemption of either class or both classes of preferred stock, the common stock, which at the organization of the company was equal in amount to the two preferred stocks, might easily come into control of the Board. Under those circumstances, unless there were ample protection thrown around the preferred stocks, and proper limitations placed upon the common stock, the preferred stocks might, by the accumulation of earnings for a period of years and then an extraordinary dividend to the common stock, be unfairly deprived of their share of the net profits. That share was to be 4% per annum "when and as determined by the Board of Directors, and only if and when the Board shall declare dividends" from the net profits, "but not exceeding four per cent". It did not cumulate, however; so that, if the company were not successful, the preferred stocks were obliged to share the misfortunes with the common stock. On the other hand, the company might be highly successful, and with the common stock in control might not pay the preferred dividends, the common stock, for the time being, foregoing its own dividends, biding its time, and then in some later year declaring a 4% dividend to the preferred stocks and an extraordinary dividend from the accumulated earnings to the common stock.

To guard against that possibility, the certificates were carefully worded in such a way as to force the common stock to declare the preferred stock dividends if they were earned. This wording, as it appears in the common stock certificates, which follows exactly the certificates of the first and second preferred stocks, with appropriate changes, is as follows:

> "If, from the business of any particular fiscal year, excluding undivided net profits remaining from previous years, after providing out of the net profits of such particular fiscal year for the payment of the full dividends for such fiscal year on the first and second preferred stock, there shall remain surplus net profits, the Board of Directors may declare, and out of such surplus net profits of such year may pay, dividends upon any other stock of the Company. But no dividends shall in any year be paid upon any such other stock out of net profits of any previous fiscal year in which the full dividends shall not have been paid on the first and second preferred stock."

Under these provisions, if full dividends on the preferred stocks were earned, but were not paid, not only was the common stock deprived of dividends in that year, but it was also deprived of the opportunity to declare out of such accumulated net profits a dividend to itself in the subsequent year. Having, however, in any particular year paid the full dividends to the preferred stocks out of the net earnings of that year, there is nothing to prevent the common stock from leaving the surplus in the treasury of the company for such declaration of dividends to the common stock in the future as the company may determine.

An illustration in figures will be helpful. The preferred stocks as issued aggregated $70,000,000, and 4% thereon required $2,800,000 annually. Assume during the first year of its history the company earned $5,000,000 and paid no dividends on any stock. During the second

year it earned $2,800,000. It might pay dividends on the preferred stocks up to, but not exceeding, 4%, or $2,800,000. The first year's earnings, $5,000,000, could not be applied to the payment of 4% on the preferred stocks in respect of the first year, since the preferred stocks are non-cumulative.

The effect of this would be to induce the common stockholders to cause the preferred dividends to be paid each year, because, if they had been paid in the first year, then there would have been $2,200,000 available for the common stock then or in any subsequent year, but, as they were not paid, the common stock would lose the right in any subsequent year to receive a dividend from such $2,200,000.

The effect of this is, furthermore, that the preferred stocks, being limited to 4%, must, nevertheless, get that 4% in each year, or else an amount equal to the net profits of that year becomes a working surplus or a segregated working fund against corporate misfortunes. But if the common stock treats the preferred stocks fairly, and pays them their full dividends, it may draw dividends at once or not, as it sees fit and at any time it sees fit.

That has been the history of the Reading Company. Beginning with dividends on the first preferred stock in 1900, soon after its reorganization, it worked them up to a 4% basis in 1903, and has thereafter paid the full dividend on the first preferred stock. It began in 1903 to pay dividends on the second preferred stock, and since then has paid those dividends in full. It then began to pay dividends on the common stock in 1905, and, beginning in 1913, and ever since, has paid dividends at the rate of 8% on the common stock (Transcript, pp. 103, 104).

And so since 1904, when Reading Company began to pay full dividends on both preferred stocks, all of the earnings over preferred dividends might have been distributed to the common stock, as the Board of Directors might declare at any time.

The preferred and common stocks, therefore, both share in the vicissitudes of the company. If the company was unsuccessful, no claims of the preferred stocks for accumulated dividends piled up against future success; and yet, if the company was successful, no machinations of the common stock, in case it should come into control, could preclude the preferred stocks from receiving their full 4% dividends while the company was piling up a surplus for future distribution to the common stock.

B. The Preferred Stock Certificates.

It is submitted that the foregoing discussion correctly states the purposes that were in view when the certificates were prepared, and places upon the terms of the stock certificates the only natural and satisfactory construction that may be placed upon them, and that this construction is fully borne out, not only by the circumstances and conditions with reference to which the certificates were drawn, but also by the conduct of Reading Company in declaring all dividends that have been declared and paid upon each class of stock of Reading Company. In the proceedings below attempts were made to place other constructions upon the stock certificates, and the appellee Reading Company argued that non-cumulative dividends, at the rate of, but not exceeding, 4% per annum in each and every fiscal year, are not the absolute limit of the rights of the prefered stocks.

Abandoning the pretense that the disposition of the interest of Reading Company in the Coal Company required by the decree is a sale, or is a distribution of a capital asset, or is a partial liquidation on partial dissolution, appellee Reading Company in its answer and cross petition (Subd. IX, Transcript, pp. 173-180) deals with this disposition according to its real nature—that is, as a disposition of accumulated surplus—and undertakes to show that, by reason of the extraordinary nature

of such disposition, the preferred stocks are entitled to share therein equally with the common stock under the terms of the preferred stock certificates.

This calls for a further discussion with reference to the authorities.

In *St. John* v. *Erie Ry. Co.,* 22 Wallace, 136, the agreement provided that

> "Said preferred stock shall be entitled to preferred dividends out of the net earnings of said road (if earned in the current year, but not otherwise), not to exceed 7% in any one year, payable semi-annually after payment of mortgage interest and delayed coupons in full."

Commenting upon this provision, this Court said (at p. 147):

> "The maximum payable on the preferred stock was specified. It might be less, or nothing. It could not be more. The amount subject to the limit prescribed depended wholly on the residue of the net earnings applicable in that way. The language employed is apt to express the relation of stockholders."

In *Scott* v. *B. & O. R. Co.,* 93 Md. 475, 49 Atl. Rep. 327, the meaning of the preference to the stockholders of that Railroad was examined exhaustively. The stock certificates set out the agreement as follows:

> "The holders of preferred stock to the amount now issued, and such additional amounts as may be lawfully issued from time to time by the President and Directors of the Company pursuant to the resolutions of the stockholders duly adopted April 11, 1899, are entitled to receive in each year, out of the surplus net profits of the Company for the current year, such yearly dividend (non-cumulative) as the Board of Directors of said Railroad Company may declare, up to but not exceeding, four per centum, before any dividend shall be set apart or paid upon the common stock."

The contention of the preferred stockholders was that they not only had the right to receive a 4% dividend before any dividend to the common stockholders, but to share *pro rata* with the common in a distribution of the residue, or, as an alternative proposition, to share equally with the common stockholders in any part of the earnings distributable after the payment of a dividend of 4% to both the common and the preferred stockholders.

It will be noted that such preferred stock was the usual 4% non-cumulative railroad stock developed at about the time of the reorganization of the Baltimore & Ohio Railroad Company, which was about the time of the reorganization pursuant to which the Reading stock certificates were issued. The dates of the two reorganizations were not far apart, and the language of the Baltimore & Ohio certificate is strikingly similar to the language of the Reading certificates.

The Court of Appeals of Maryland, after the presentation of the case exhaustively by counsel among the most eminent in the country, decided that the preferred stockholders, after receiving a dividend of 4% in any one year, were not entitled to share with the common stockholders in the distribution of the residue of the net earnings, either equally or after the payment of a like dividend to the common stockholders, but that the preferred stockholders were entitled to a dividend of 4%, and no more, upon the payment of any dividend to the holders of the common stock.

In the disposition by the Union Pacific Railroad Company of its interest in the Southern Pacific Company, the Union Pacific and its counsel were always alive to and observant of the respective reights of their preferred and common stockholders. They made no attempt to dispose of the interest in the Southern Pacific Company through a so-called sale to the stockholders, preferred and common, share and share alike, at a purely arbitrary figure

and grossly inadequate price, and thus permit the preferred stockholders to reap the benefit of the difference between the value of what they received and the price paid for it. Instead, as heretofore pointed out, *the disposition was an actual sale at approximately the market price, and the proceeds of that sale were placed in the treasury of the Union Pacific Railroad Company.* In other words, the method of disposition and the treatment of the proceeds were in accordance with the suggestion for the modification of the Plan made mandatory by the decree that these appellants submitted to the District Court and that is explained at length under III hereof.

After the proceeds had come into the treasury of the Union Pacific Railroad Company, it declared a special dividend of $80,000,000 payable to the common stock, to the exclusion of the preferred stock.* The Union Pacific stock certificates set out the agreement as follows:

> "Such preferred stock shall be entitled, in preference and priority over the common stock of said corporation, to dividends in each and every fiscal year, at such rate, not exceeding four per cent. per annum, payable out of net profits, as shall be declared by the Board of Directors. Such dividends are to be non-cumulative, and the preferred stock is entitled to no other or further share of the profits."

Thereupon the holder of a large amount of the preferred stock brought an action against the Union Pacific Railroad Company to restrain the payment of this extra dividend to its common stockholders. The controversy was finally determined by the Court of Appeals of the State of New York (*Equitable Life Assurance Society* v. *Union Pacific R. R. Co.*, 212 N. Y. 360).

The Court, in an exhaustive opinion by Hiscock, *J.*, now Chief Judge, held that the preferred stockholders,

*Of this $80,000,000, upwards of $58,000,000 was the profit from the disposition of the interest in the Southern Pacific Company.

having received their 4% dividends, were at an end of their rights so far as profits were concerned.

It has been urged, however, that the rule as announced in *St. John* v. *Erie Ry. Co.* (*supra*); *Scott* v. *B. & O. R. Co.* (*supra*), and *Equitable Life Assurance Society* v. *Union Pacific R. Co.* (*supra*) is not the rule in the State of Pennsylvania, and that the Pennsylvania rule is that where in the agreement there is nothing limiting the right of the preferred stockholders to a specified dividend, they are entitled to share with the common stockholders in profits distributed after the latter have received in any year an amount equal to the dividend on the preferred stock. This rule is peculiar to Pennsylvania, and is not sustained in other jurisdictions.

In *Stone* v. *United States Envelope Co.*, 111 Atl. Rep. 536, the Supreme Judicial Court of Maine had before it a contention of the preferred stockholders that where a preferred stock is created *with no stipulation in reference to participation in surplus,* the balance of the profits, after payment of a 7% dividend to the preferred stock, and perhaps an equal dividend to the common stock, must all go to the stockholders, both preferred and common, without discrimination.

With reference to this, the Court says (p. 537):

> "Both parties present authorities sustaining their respective contentions. There are two opposing theories, each of which has judicial support. One theory is that the preferred stockholder presumptively yields nothing in compensation for the benefits which he receives; that he has and holds all the rights of the common shareholder and in addition has his preferential rights.
>
> * * * * * *
>
> The other theory, which we believe to be better and supported by the weight of authority, is that, in receiving the greater security of his preferential rights, the preferred stockholder impliedly agrees to accept such rights in lieu of equal participation."

Where, however, the right of the preferred stockholders is limited to a specified dividend, as in the Reading Company stock certificates, the Pennsylvania rule does not operate.* But the appellee Reading Company insists that, despite the fact that its preferred stockholders are limited to a specified dividend, and that the Pennsylvania rule does not apply, the preferred stockholders of Reading Company, on grounds that are common to all jurisdictions, are entitled to participate equally with its common stockholders in the disposition of its interest in the Coal Company, by reason of the fact that the limitation of the preferred stockholders to a specified dividend cannot be applied to this distribution, because its extraordinary nature takes it out of the class of distributions to which this limitation applies. This is set forth in the answer and cross petition of appellee Reading Company, as follows:

> "The Reading Company is advised and believes that the holders of the preferred stock are entitled to a preference and are subject to a limitation of four per cent. per annum with respect to dividends from current profits of the Reading Company; but that they are entitled to no preference and are subject to no limitation with respect to distribution either of capital or of accumulations of profits which, for any reason, have become part of the capital or partake of the nature of capital and are not being detached therefrom by any voluntary act of the Company but only by a compulsion that makes such detachment a distribution of assets in partial liquidation of the corporation" (Transcript, p. 174).

*In the proceedings in the District Court a number of Pennsylvania decisions were cited by counsel for the appellee Reading Company and the appellees Adrian Iselin *et al.* and William B. Kurtz *et al.*, representing preferred stockholders. These decisions are not deemed important by these appellants, for the reason that most of them deal with situations where the right of the preferred stockholders was not limited to a specified dividend, thus permitting the Pennsylvania rule to operate, and the others are not in point. As said appellees, however, attach importance to these decisions, they are discussed in Appendix A hereto.

Such a contention is made possible solely by the provisions of the Plan made mandatory by the decree to which these appellants object. If the Plan should be modified in accordance with the suggestions offered by these appellants so as to bring about a *bona fide* sale at approximately market value and the placing of the proceeds of the sale in the treasury of Reading Company, as was done in the *Union Pacific* case, or so as to bring about a *bona fide* disposition of capital assets and the reduction of the capital stock to the extent of the appraised value of those assets, the foregoing contention could not be advanced.

Reading Company is to detach from its assets, and dispose of, its interest in the Coal Company under compulsion of the mandate of this Court, and that is as far as the compulsion goes. The choice of means for disposing of such interest, within limits which are not important in this connection, has been left absolutely to the voluntary act of Reading Company. The answer and cross-petition of Reading Company practically admits this in the following language:

> "Though in an important sense compulsory because taken under pressure of necessity created by the decree of this Honorable Court, the plan must be regarded as in some sense also voluntary since it requires corporate action not directly involved in the issues in this cause" (Transcript, p. 155).

But the Reading Company, as its own free and voluntary act, has devised a Plan for such disposition that operates to the prejudice of the rights of the common stockholders, and has endeavored to fasten the responsibility for such prejudice upon the compulsion of the mandate of this Court. In other words, the foregoing contention is based upon a situation that Reading Company has created by its own voluntary act, and it is now attempting to use the situation that it has created as a justification for creating it.

This may, perhaps, be made clearer by pointing out that, if an actual *bona fide* sale at approximately the market value were made of the interest of Reading Company in the Coal Company, no questions involving distribution of capital assets, or partial liquidation on partial dissolution, or extraordinary and compulsory distributions of assets would be involved. There would merely be the sale of an asset and the substitution of its proceeds for the asset itself among the assets of Reading Company, with such charge to surplus, if any, as might be necessary to adjust the difference between the value at which the asset was carried on the books of the Reading Company and the proceeds of its sale. If the Reading Company should make a *bona fide* sale, whether voluntary or by compulsion, of any of its assets, in this case or in any other case, its common stockholders could have no objection to the charge to its surplus of the legitimate loss that would arise under such a sale.

The extraordinary distribution of surplus that is involved in this case, and that is claimed by Reading Company to be outside the specified dividend to which the preferred stocks are limited, has been created artificially by the device in the Plan that is intended to bring about a so-called sale of the interest of Reading Company in the Coal Company at an inadequate price.

It is not conceded, however, that, even if such an extraordinary distribution from surplus as is here involved were made necessary by the mandate of this Court, the limitation of the right of the preferred stockholders to a specified dividend would not apply thereto.

Diligent search has failed to disclose any decisions of the Pennsylvania courts regarding such distributions, except the following:

In *City of Allegheny* v. *Pittsburgh, A. & M. P. Ry. Co.*, 179 Pa. St. 414; 36 Atl. Rep. 161, the defendant was chartered by a special act by the provisions of which it

was to declare dividends of "so much of the profits of said company as shall appear advisable to the directors thereof", but in no case to exceed the amount of the net profits of the company, and was required also to pay to the City of Allegheny a certain percentage "of the dividends declared". Defendant held certain stock of a second corporation, which was exchanged for stock in a third corporation, and the latter stock was then issued directly to defendant's stockholders. It was held that the transaction was a severance of the stock from the body of the corporate property and a distribution of its value or equivalent among the stockholders individually, and therefore a dividend taxable, unless the legislative intent was to restrict to cash dividends only, the burden of proof of which would be upon the appellant. While this case involved a tax question, and did not deal with the respective rights of preferred and common stockholders, it clearly indicates the view of the Pennsylvania Supreme Court that a dividend made under unusual circumstances, and consisting of assets of a permanent character, is not to be differentiated from any other dividends.

The decisions of courts in other jurisdictions and decisions of the Federal courts are to the effect that the limitation of preferred stock to a specific dividend applies to extraordinary as well as to ordinary distributions from surplus.

In *Equitable Life Assurance Society* v. *Union Pacific R. R. Co., supra,* Hiscock, *J.,* now Chief Judge, writing for a unanimous Court except one Judge not sitting, says, at page 366:

> "When a corporation is organized it secures capital by the issue of shares of capital stock. The fund or property thus secured answers the two-fold purpose of furnishing means for carrying on the operations of the corporation and also security for the payment of creditors. This capital stock is carried as a liability and universally, so far as I am aware,

at its par amount. It is thus carried as a liability because this is the proper bookkeeping entry. But aside from this, such entry also serves to emphasize the duty of the corporation to keep its capital stock unimpaired for the protection of those dealing with it. If the operations of the corporation result in gains, such gains are carried to the credit, not of the capital stock account but of some other account, as surplus or profit and loss. Of course they may be capitalized by the issue of stock against them and sometimes in the cases of certain corporations like banks or insurance corporations where a certain ratio between assets and liabilities other than to capital stock is required, such surplus or profits may be counted and maintained as capital although not formally capitalized.

In the absence of some such special consideration I think we may take notice that it is the ordinary rule of corporate management established by decisions, statutes and business usages that the surplus of these gains or profits beyond what may be necessary to keep good the liability to capital stock which has been issued, may, in the discretion of a board of directors, be distributed amongst its stockholders as dividends and returns on their investment. Such being the general rule, it is incumbent on the plaintiff to show that there is something so peculiar in the two transactions being considered that the profits resulting therefrom are of a different nature in respect of this subject than those ordinarily realized in corporate business, and I think it has failed to do this."

In undertaking to show that there was something so peculiar in the profits realized from the sale of the interest of the Union Pacific in the Southern Pacific, out of which profits the dividend involved had been declared to the common stockholders to the exclusion of the preferred stockholders, that those profits were of a nature different from those ordinarily realized in corporate business, and were not, therefore, subject to the limitation upon the preferred stocks, the plaintiff pointed out that the Union Pacific Railroad Company was not organized to deal in

stocks, and that, therefore, the profits derived from the sale of the Southern Pacific stock which it held among its assets were not profits ordinarily realized in corporate business. The Court held that the profits derived from the sale of the Southern Pacific stock were accumulated profits from surplus, and rejected the proposition that these amounts, because resulting from what was, perhaps, an unusual transaction, were not profits, but, as contended by that plaintiff, an accretion which belonged to capital. The opinion states:

> "No case has been cited which in my opinion sustains the proposition that these gains must be treated as an accretion to capital and distributed as such, rather than as profit distributable in the discretion of the directors in dividends."

Much more emphatic is the situation in the instant case. The Union Pacific Railroad Company was and is an operating railroad company. The Reading Company is a proprietary and not an operating company. In the *Equitable-Union Pacific* case it was strenuously contended that the accretion realized from the sale of some stocks which the railroad company had in its treasury could not have been within the contemplation of the railroad's charter, and, therefore, that such profits could not have been in the mind of the preferred shareholders when they agreed to take 4% dividends in full for their share of profits.

But no such contention is tenable here. The corporate powers of Reading Company are practically unlimited, except that it may not have banking privileges or franchises or the privilege of issuing its obligations as money. The assets of Reading Company consist of railroad and floating equipment, which it leases and receives the rentals thereon; of bonds and stocks; of a debt from one of its subsidiaries, the Coal Company; and of cash and other current items. If it acquires a block of stock for a

certain price, and subsequently disposes of it for an increased price, that increase is just as much earnings as though the corporation whose stock was sold had declared a dividend to the Reading Company as stockholder. Its charter gives it the right to acquire, enjoy and dispose of all manner of property, specifically securities.

In the earlier case of *Williams* v. *Western Union Telegraph Co.*, 93 N. Y. 162, the Court said:

> "By loss or misfortune, or misconduct of the managing officers of a corporation, its capital stock may be reduced below the amount limited by its charter; but whatever property it has up to that limit must be regarded as its capital stock. When its property exceeds that limit, then the excess is surplus. Such surplus belongs to the corporation and is a portion of its property, and, in a general sense, may be regarded as a portion of its capital, but in a strictly legal sense it is not a portion of its capital, and is always regarded as surplus profits. The very section we are considering contemplates that there may be a surplus, and that such surplus may be divided. The surplus may be in cash, and then it may be divided in cash; it may be in property, and if the property is so situated that a division thereof among the stockholders is practicable, a dividend in property may be declared, and that may be distributed among stockholders. All such dividends diminish and deplete the property of the corporation, and that section was designed to prevent dividends of property which tended to deplete the assets of the company below the sum limited in its charter as the amount of its capital stock" (at pp. 188, 189).

That case drew no distinction between ordinary and extraordinary distributions, although an extraordinary distribution was there under consideration.

In *Russell* v. *American Gas & Electric Co.*, 152 App. Div. 136; 136 N. Y. Supp. 602, the Appellate Division of the Supreme Court, for the First Department, had before it the appeal of the holder of 480 shares of the preferred

stock of the defendant corporation, which had an authorized capital stock of $7,000,000, divided into 140,000 shares, of the par value of $50 each, one-half of which was preferred and one-half common. There were 36,770 shares of preferred and 20,000 shares of common unissued. The preferred stock was entitled to accumulated dividends at the rate of 6 per cent. per annum and to preference in the distribution of assets until the par value and accumulated dividends had been paid and "to no further dividend or distribution."

The directors of the defendant corporation resolved to issue 10,000 shares of the unissued common stock and to allow the holders of the issued common stock to subscribe for the same, ratably, at par. The market value of the common stock was then about $80 per share, while that of the preferred was about $47. The plaintiff demanded that he be allowed to subscribe *pro rata* for the common stock, along with the then holders of common stock. His request was refused and he thereupon commenced his action. The Court below denied his motion for an injunction *pendente lite*, but upon condition that he be allowed to subscribe for an equivalent amount of *preferred stock* at par. He then took this appeal. The Court, after stating the facts as above, said:

> "The principal ground of plaintiff's alleged cause of action, as set forth in his complaint, is that the holders of the common stock have been given the right to subscribe, at par, for stock which is worth about thirty dollars more than par, while the same right has not been extended to the holders of the preferred stock. I am unable to see how the plaintiff can maintain his alleged cause of action, or that he has any reason to complain. Where a corporation has property in excess of the amount of its capital stock, the excess is surplus which may be divided among the stockholders entitled to share therein, either in money or property. (*Williams* v. *Western Union Telegraph Co.*, 93 N. Y. 162.) As a holder of the preferred

stock the plaintiff could claim no interest in such excess. So long as the dividends upon his stock were paid, and the defendant had property equal in value to the amount of its outstanding capital stock, after the payment of its debts, the corporation, if it saw fit to do so, could distribute all the rest of its assets among the holders of its common stock and the plaintiff would have no ground for complaint.

"* * * whatever value the stock had above par represented surplus and was available for distribution among the holders of its common stock. Whether this was done by selling the stock at its market value and then distributing the excess, or by issuing the stock to the holders of the common at par, does not concern the plaintiff. He cannot insist that the corporation build up a large surplus nor object to a distribution of its property, when duly authorized, among the holders of common stock, so long as his dividends are paid and its capital remains unimpaired.

"It is urged, however, and with some force, that the plaintiff, as a stockholder, had the right to share proportionately in any issue of stock * * *. In so far as this contention is based upon plaintiff's asserted right to participate in the profits derived from the issue of the common stock below its market value, it is unsound and cannot be sustained."

The Court below had given plaintiff the right to subscribe enough *preferred* stock to preserve his proportionate interest in the Company, and this was not disturbed on appeal.

It will be noted that in this case the new stock was to be subscribed for *at par,* and that no encroachment on surplus or distribution of assets was, therefore, involved.

The rule of this case may be stated to be that, so long as his dividends are paid and the capital of the corporation remains unimpaired, a prefered stockholder cannot object to a distribution of its property among the common stockholders. This rule would apply to an extraordinary

distribution out of the surplus, such as the appellee Reading Company claims is not within the limitation of its preferred stock certificates, but it goes even beyond that in excluding the prefered stock from *any benefit* in which the common stock may participate so long as the preferred dividends are paid and the capital of the corporation remains unimpaired.

In *Niles* v. *Ludlow Valve Mfg. Co.,* 202 Fed. 141, the Board of Directors of the defendant company had determined to make a distribution of accumulated surplus by way of a stock dividend, and the plaintiff, who was administrator and represented 100 shares of preferred stock, insisted that he was entitled to share in this division of accumulated surplus. The preferred stock was entitled to "receive interest or dividends of 8 per cent. per annum and be preferred as to capital as well as to dividends". Dividends had been paid by the defendant corporation for twenty years, and in almost every instance the dividend on the common stock had been larger than on the preferred stock, without any objection on the part of the prefered stockholders, including the plaintiff and his intestate. This is analogous to the history of the Reading Company since 1905.

The opinion states (p. 142):

> "that the question turns upon who owned the $500,000 accumulated by the defendant prior to the time the stock dividend was declared"

and continues:

> "It seems evident that as these profits arose from year to year, the Board of Directors might properly have divided them annually, as dividends, among the common stockholders. We think they might legally have done this, and, if so, it is not easy to understand how the common stockholders lost these rights because the Board reserved the division until the surplus had reached the sum of $500,000. The fund,

large or small, belonged to the common stockholders and whether they received cash, or certificates which represented cash, is immaterial. These stockholders have the burden of administration upon them; if the corporation is unsuccessful, the loss falls upon them; if successful, they receive the benefits. We think that when the preferred stockholders receive the large interest of 8% provided for in the certificate they receive all to which they are entitled from the income of the corporation * * * Upon what principle of law or equity should they be permitted to share in surplus earned by the corporation when they are exempted from bearing any of the loss incurred? Before a dollar can be paid as a dividend to the common stockholder, the entire 8% must be paid to the preferred stockholders. In addition to these advantages, it is now asserted that though they bear no share of the burden when the business is unsuccessful, they should share equally with the common stockholders when it is prosperous * * * Once admit that the preferred stockholder is entitled to share in the surplus after his preferred dividend is paid, and it follows as an inevitable conclusion that he shares on equal terms with the common stockholder" (at pp. 143, 144).

Whatever may be the rule where there is no limitation in the contract, we know of no authority, and can find none, which holds that anything may be distributed to the preferred stockholders from the surplus of the corporation after they have received their full agreed dividends where the language of the certificate affirmatively provides that such dividends are the limit of their rights.

The stock certificates of the Reading Company do so affirmatively provide in the most exact and emphatic language. The prefered stocks are "entitled to non-cumulative dividends at the rate of, *but not exceeding* four per cent. per annum, in each and every fiscal year". And then, to emphasize the language, the certificate goes

on to provide that such dividends are payable *only* from undivided net profits of the company when and as determined by the Board of Directors and only if and when the Board of Directors shall declare dividends therefrom. The use of the word "only" may quite properly be construed to mean that the undivided net profits of each fiscal year are the sole source to which the preferred stocks may look for even the four per cent. non-cumulative dividends to which they are entitled.

IX.

The holders of the common stock of Reading Company are absolutely entitled to distributions out of surplus net profits of the Reading Company of years other than those for which the full dividends shall not have been paid on the first and second preferred stock.

It has been shown under VIII that the preferred stockholders of Reading Company are absolutely limited to non-cumulative dividends at the rate of, but not exceeding four per cent. per annum in each and every fiscal year, and that there is no foundation in law for the proposition that, when a distribution of surplus is made in an extraordinary amount or under extraordinary conditions, such limitation does not apply to the preferred stocks, and that they are entitled to share therein equally with the common stocks. It follows, therefore, that any distribution from surplus, made after the preferred stock-

holders have received in full the dividends to which they are limited by the certificates, must be made solely to the common stockholders and to the exclusion of the preferred stockholders. And this is fully supported by the authorities that have been reviewed:

St. John v. *Erie Railway Co., supra;*
Scott v. *B. & O. R. Co., supra;*
Equitable Life Assurance Society v. *Union Pacific R. Co., supra;*
Williams v. *Western Union Telegraph Co., supra;*
Russell v. *American Gas & Electric Co., supra;*
Niles v. *Ludlow Valve Mfg. Co., supra.*

The appellee Reading Company in its answer and cross petition, however, insists that

> "There is to be no dividend or distribution of the coal stock. The situation is not such as to justify declaring a dividend in respect of the coal stock. No extraordinary dividend has been or will be declared by the Reading Company. The common stockholders cannot force a dividend nor can the sale be treated as if a dividend had been declared" (Transcript, p. 162).

And, further,

> "Common stockholders have no right in earnings until that right has been created by the declaration of a dividend and they have no right to require a dividend to be declared in the absence of bad faith on the part of the Board of Directors" (Transcript, p. 165).

And still further,

> "If, however, contrary to the views above expressed, the plan were to be regarded as involving a

distribution of surplus, as is contended by the Prosser Committee, the preferred stockholders should not with fairness, and could not rightfully, be excluded from participation in it, because it would be neither a dividend nor a voluntary distribution of current surplus net profits" (Transcript, p. 173).

These appellants concede that the common stockholders have no right to require a dividend to be declared in the absence of bad faith on the part of its Board of Directors. They do insist, however:

1. That the so-called sale of the interest of Reading Company in the Coal Company required by the decree is not, and is not intended to be, a sale in any real sense;

2. That this so-called sale, in its purpose and effect, and in everything but form and name, is, and is intended to be, a dividend or distribution of surplus net profits;

3. That, in substance and in fact, the action of the Board of Directors in presenting and procuring the approval of the Plan pursuant to which the disposition by Reading Company of its interest in the Coal Company is to be made was, and was intended to be, the declaration of a dividend, although it did take, and was intended to take, the form and name of a sale;

4. That, in view of this, the preferred stockholders may not with fairness, and cannot rightfully be permitted to, participate in such distribution;

5. That such action on the part of the Board of Directors of Reading Company was purely voluntary;

6. That there is nothing in the mandate of this Court that interfered with the choice of the Board of Directors of Reading Company as among

(*a*) Disposing of the interest of Reading Company in the Coal Company by making a *bona fide* sale thereof and placing the proceeds in the corporate treasury.

(*b*) Distributing such interest as a distribution of capital and reducing the capital stock, preferred and common, share and share alike, by the appraised value of such distribution; and

(*c*) Distributing such interest to the stockholders as a dividend; and

7. That the Board of Directors of Reading Company having made the choice of distributing its interest in the Coal Company as a dividend, such dividend must be distributed to the holders of common stock, to the exclusion of the preferred stock.

X.

The disposition of the interest of Reading Company in the stock of the Coal Company required by the decree confers upon the holders of the preferred stock of Reading Company a benefit to the prejudice of the legal rights of the holders of the common stock of Reading Company.

Respectfully submitted,

ROBERTS WALKER,
Counsel for Seward Prosser, Mortimer N. Buckner and John H. Mason, as a Committee, etc., Appellants.

J. DUPRATT WHITE,
JOSEPH M. HARTFIELD,
ALLEN MCCARTY,
of Counsel.

Appendix A.

PENNSYLVANIA DECISIONS.

In the proceedings in the District Court the following Pennsylvania decisions were cited by counsel for the appellee Reading Company and the appellees Adrian Iselin *et al.* and William B. Kurtz *et al.*, representing preferred stockholders:

North American Mining Co. v. *Clarke*, 40 Pa. 432 (1861).

In this case the controversy was between the holders of assessable and non-assessable shares of a mining company upon *final liquidation.* The holders of the shares that had been assessed claimed that, under certain provisions of the stock contract providing for refunds of assessments out of surplus, their assessments should be refunded to them, and that the remainder should be distributed to all shares alike. *There was no surplus,* and the Court held that the distribution should be to all shares alike, without reference to the claim of the holders of the assessed shares.

Vinton's Appeal, 99 Pa. 434 (1882).

In this case a gas company sold a part of its corporate property and distributed the proceeds as a dividend. The controversy was between the life tenant and a remainderman of a block of stock over the division of the dividend between them. *No question of the respective rights of preferred and common stockholders was involved.*

Fidelity Trust Co. v. *Lehigh Valley R. Co.*, 215 Pa. 610; 64 Atl. Rep. 829 (1906);

Sternbergh v. *Brock*, 225 Pa. 279; 74 Atl. Rep. 166 (1909);

Sterling v. *H. F. Watson Co.*, 241 Pa. 105; 88 Atl. Rep. 297;

Englander v. *Osborne*, 261 Pa. 366; 104 Atl. Rep. 614 (1918).

In each of these cases the preferred stock was *cumulative* and contained no limitation to a specified dividend in each and every fiscal year, such as is contained in the Reading Company preferred stock certificates. Consequently, the controversy between the preferred and common stockholders called for the application by the Court of the rule that is peculiar to Pennsylvania and that has been heretofore discussed.

Pardee v. *Harwood Electric Co.*, 262 Pa. 68; 105 Atl. Rep. 48 (1918).

In this case the holders of the preferred stock were entitled to receive *cumulative* dividends at the rate of 6 per cent. per annum, and the stock contract further provided that dividends at that rate *must* be declared by the Board of Directors, when earned, to the extent of and only from the undivided net earnings in each and every fiscal year in preference and priority to any payment in or for such fiscal year over any dividend on other stock.

The preferred stockholders sought to compel the payment of dividends required by the mandatory provision of the stock contract, but the Court held that the discretion of the directors of the corporation could not be overridden by this mandatory provision. The decision in the case may be summarized as follows:

(1) The owners of the preferred stock in a corporation are stockholders and not creditors;

(2) A public service corporation is not required to declare such dividends as will destroy or impair its efficiency; and

(3) The corporation cannot so contract with the holders of its preferred stock as to destroy its usefulness as a public service corporation.

The foregoing brief summaries of the decisions in these cases are sufficient to make it clear that they have no bearing upon the issues in this appeal.

IN THE

SUPREME COURT of the UNITED STATES

OCTOBER TERM, 1921
No. 609

CONTINENTAL INSURANCE COMPANY and FIDELITY-PHENIX FIRE INSURANCE COMPANY OF NEW YORK

Appellants

against

READING COMPANY and Others

Appellees

No. 610

SEWARD PROSSER, MORTIMER N. BUCKNER and JOHN H. MASON, as a Committee, etc.

Appellants

against

READING COMPANY and Others

Appellees

APPEALS FROM THE DISTRICT COURT OF THE UNITED STATES FOR THE EASTERN DISTRICT OF PENNSYLVANIA

BRIEF FOR READING COMPANY ON REARGUMENT

CHARLES HEEBNER
R. C. LEFFINGWELL
WM. CLARKE MASON
L. D. ADKINS
A. I. HENDERSON
Of Counsel

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APPEALS FROM THE DISTRICT COURT OF THE UNITED STATES FOR THE EASTERN DISTRICT OF PENNSYLVANIA

BRIEF FOR READING COMPANY ON REARGUMENT

This cause originated as a proceeding by the Government of the United States to dissolve the intercorporate relations existing between the corporate defendants on the ground that such relations constituted a violation of the Sherman Anti-Trust Act (26 Stat. 209), and also

of the commodities clause of the Act of Congress of June 29, 1906 (34 Stat. 584, 585) (Record, p. 2).

On April 26, 1920, this Court handed down its opinion (253 U. S. 26), holding that the combination existing and maintained through the Reading Company was unlawful.

References and Designations

The original record in the dissolution proceedings is filed in this Court as Nos. 3 and 4 of October Term, 1919, and is referred to in this brief as the Old Record, to distinguish it from the Record on these appeals.

For convenience the following designations adopted in this Court's opinion (253 U. S. 41) are adopted in this brief:

> The present Reading Company is called the Holding Company;
>
> Philadelphia and Reading Railway Company is called Reading Railway Company;
>
> The Philadelphia and Reading Coal and Iron Company is called Reading Coal Company;
>
> The Central Railroad Company of New Jersey is called Central Railroad Company;
>
> The Lehigh and Wilkes-Barre Coal Company is called Wilkes-Barre Coal Company.

The future Reading Company, after its reorganization as a railroad corporation and merger of the Reading Railway Company, as provided in the decree, is called the New Railway Company.

The new corporation which is to acquire the equity in the stock of the Reading Coal Company, as provided in the decree, is called the New Coal Company.

Seward Prosser, Mortimer N. Buckner and John H. Mason as a Committee, etc., appellants, are called the Prosser Committee.

Continental Insurance Company and Fidelity-Phenix Fire Insurance Company of New York, appellants, are called the Insurance Companies.

Past History

The salient facts of the history of the corporate defendants as found by this Court are stated in the following excerpts from its opinion (253 U. S. 44-51):

"The Philadelphia & Reading *Railroad* Company was chartered by special act of the Pennsylvania General Assembly in 1833, and it conducted the business of a railroad carrier prosperously for about thirty years, when, as its annual reports show, it embarked upon the policy of attempting to control the anthracite tonnage of the Schuylkill field by acquiring extensive ownership of coal lands. Thus, the report of the Company for 1871 contains the following:

> "'Up to this time about 70,000 acres of the best anthracite coal lands in Pennsylvania have been acquired and will be held by an auxiliary company, known as the Philadelphia and Reading Coal and Iron Company, of which the Philadelphia and Reading Railroad Company *is the only stockholder.* The result of this action has been to secure—and *attach to the company's railroad*—a body of coal land capable *of supplying all the coal-tonnage that can possibly be transported over the road for centuries.*'

* * * * * * * *

"In the large financial operations incident to the expansion policy thus described, bonds were issued, secured by a mortgage on all of the property of the Reading Railroad Company and of the Reading Coal Company. In 1893 there was default in the payment of interest on these bonds and receivers were appointed who operated both properties until 1896 when they were sold to representatives of the creditors and stockholders of the two companies, and under a scheme of reorganization, the validity of which is assailed in this suit, both properties were transferred to three corporations in the manner now to be described:

"1st. To the Reading *Railway* Company, a corporation newly organized under the laws of Pennsylvania, were allotted about 1,000 miles of the railroad (but none of the equipment) which had been owned or leased by the former Reading *Railroad* Company. The capital stock of this Company was fixed at $20,000,000 and it issued $20,000,000 of bonds, all of which were given to the Holding Company.

* * * * * * * *

"2nd. By the decree of sale the Reading Coal and Iron Company was released from its former obligations and to it thus freed the principal part of the property (coal and other), owned by it before the sale, was allotted and re-transferred upon condition, that it would deliver all of its capital stock to the Holding Company, would become co-obligor with that company on bonds to be issued, and would join with it in executing a mortgage for $135,000,000 on all of its property to secure such bonds.

* * * * * * * *

"3rd. To serve the purposes of the intended Holding Company, a charter granted in 1871 by special act of the General Assembly of Pennsylvania, but unused for twenty years, was utilized. This charter was of the class denominated "omnibus" by the Supreme Court of Pennsylvania, and in terms it authorized the company to engage in, or control, almost any business, other than that of a bank of issue,—this broad charter was the occasion for making use of the company in this enterprise.

* * * * * * * * *

"* * * the Holding Company * * * became the owner of the title to railway equipment, real estate, colliers and barges of an estimated value of $34,400,000; plus all of the capital stock and bonds of the new Railway Company, $40,000,000; plus all of the capital stock of the Coal Company, $8,000,000, and a contract by that company to mortgage, for the use of the Holding Company, its entire property; plus other stocks, bonds and mortgages, owned by the former Railroad Company of the estimated value of over $38,000,000—making a total value, as repre-

sented at the time to the New York Stock Exchange, of $193,613,000.

"Thus this scheme of reorganization * * * made the Coal Company and the Railway Company mere agents or instrumentalities of the Holding Company—the mining and transportation departments of its business—for producing, purchasing, and selling coal and for transporting it to market. The Reading *Railway* Company and the Reading Coal Company each had thereafter but one stockholder—the Holding Company—and their earnings were to be distributed not in proportion to the shares of their capital stocks, aggregating $28,000,000, but were to go to the creditors and shareholders of the Holding Company, with its mortgage debt of $135,000,000 and its capital stock of $140,000,000. The Holding Company thus served to pool the property, the activities and the profits of the three companies."

* * * * * * * *

"* * *, the Holding Company, in January, 1901, purchased a controlling interest in the capital stock of the Central Railroad Company. When this suit was commenced that company was operating 675 miles of track, over which it carried in 1913, 10,783,000 tons of anthracite,—almost one-half of its total freight traffic. Its capital stock was then $27,436,000 and its funded debt was $46,881,000.

"This Central Company owned, at the time, in excess of eleven-twelfths of the capital stock of the Wilkes-Barre Coal Company, with a capital stock of over $9,000,000 and a funded debt of about $17,000,000. And that company owned or had leased in excess of 14,000 acres of coal bearing lands—13,000 acres in the Wyoming field—and in the year ending June 30, 1913, it shipped from its lands thus owned or controlled, 6,243,000 tons of coal, which was sold for over $20,000,000."

The Decision of this Court

This Court found that the Holding Company was in active, dominating control of the Reading Railway Company and of the competing Central Railroad system, and also of the two coal companies, the Reading Coal Company

and the Wilkes-Barre Coal Company, and that the combination thus maintained constituted a violation of the Anti-Trust Act and fell within the condemnation of the commodities clause. (253 U. S. 59-63.)

Accordingly this Court directed the District Court to enter a decree

> "dissolving the combination of the Reading Company, the Philadelphia and Reading Railway Company, the Philadelphia and Reading Coal and Iron Company, the Central Railroad Company of New Jersey and the Lehigh and Wilkes-Barre Coal Company, existing and maintained through the Reading Company, with such provision for the disposition of the shares of stock and bonds and other property of the various companies, held by the Reading Company, as may be necessary to establish the entire independence from that company and from each other, of the Philadelphia and Reading Railway Company, the Philadelphia and Reading Coal and Iron Company, the Central Railroad Company of New Jersey and the Lehigh and Wilkes-Barre Coal Company, and also that such disposition shall be made by the decree of the stocks and bonds of the Lehigh and Wilkes-Barre Coal Company, held by the Central Railroad Company of New Jersey, as may be necessary to establish entire independence between these two companies to the end that the affairs of all of these now combined companies may be conducted in harmony with the law."

The Interlocutory Decree of the District Court

The Mandate of this Court was filed in the District Court on August 13, 1920 (Record, p. 27), and thereafter on October 8, 1920, the District Court entered a Decree on Mandate (Record, p. 31), which among other things ordered that

> "the defendants shall submit to this Court a plan for the dissolution of the unlawful combination between the Reading Company, the Philadelphia & Reading Railway Company, the Philadelphia &

Reading Coal and Iron Company, the Central Railroad Company of New Jersey and the Lehigh & Wilkes-Barre Coal Company, existing and maintained through the Reading Company, with such provision for the disposition of the shares of stock and bonds and other property of the various companies, held by the Reading Company, as may be necessary to establish the entire independence from that company and from each other, of the Philadelphia & Reading Railway Company, the Philadelphia and Reading Coal and Iron Company, the Central Railroad Company of New Jersey and the Lehigh & Wilkes-Barre Coal Company, to the end that the affairs of all these now combined companies may be conducted in harmony with the law." (Record, p. 36.)

The Situation at the Time of the Interlocutory Decree

The Holding Company has a special charter under the laws of Pennsylvania granted prior to the adoption of the Constitution of 1874, with particularly broad powers. Copies of its charter, and of the charter of the Pennsylvania Company therein incorporated by reference, are printed in the Record, pp. 189-197. The Holding Company is not a common carrier and is not subject to regulation by Federal or State authorities having jurisdiction over railroads. The Holding Company owned:

(a) $42,481,700 par value, being the entire capital stock (Record, p. 157), and $20,000,000 bonds (Record, p. 114), of the Reading Railway Company;

(b) $8,000,000 par value, being the entire capital stock of the Reading Coal Company (Record, p. 157);

(c) real estate, rolling stock and floating equipment used upon or in connection with the Reading railway system (Record, p. 200);

(d) shares of stock and bonds of other railroads and terminal companies constituting part of the Reading railway system (Record, pp. 200, 232; Old Record, pp. 1298-1300);

(e) the entire capital stock of the Reading Iron Company par value, $1,000,000 (estimated value according to Moody's market letter, $22,791,500, Record, pp. 123, 232);

(f) $14,504,000, par value, being more than a majority of the stock of the Central Railroad Company. All the stock of the Central Railroad Company (except 40 shares) owned by the Holding Company is pledged under the Collateral Trust Mortgage of the Holding Company to the Pennsylvania Company for Insurances on Lives and Granting Annuities, Trustee, dated April 1, 1901. The bonds issued by the Holding Company under this mortgage bear interest at 4%, mature April 1, 1951, and are redeemable before maturity at 105 per cent. of the par value thereof and accrued interest. Bonds to the amount of $23,000,000 are issued and outstanding (Record, p. 158).

The Central Railroad Company owned more than ninety per cent. of the capital stock of the Wilkes-Barre Coal Company. (Record, p. 23.)

The issued and outstanding capital stock of the Holding Company is as follows (Record, p. 157):

4% non-cumulative First Preferred Stock	$28,000,000.00
4% non-cumulative Second Preferred Stock	42,000,000.00
Total Preferred Stock	$70,000,000.00
Common Stock	70,000,000.00
Total Capital Stock	$140,000,000.00

The preferred stock has full voting power (Record, p. 181). The stock certificates are set out in full in the Record, pp. 82-93. There is no material difference between the certificates originally issued at the time of the reorganization in 1896, set out on pages 82-87 of the Record, and the certificates now in use, set out on pages 88-93, nor, for

the purposes of these appeals, between the first and second preferred stocks.

The Holding Company and the Reading Coal Company are joint obligors under the General Mortgage to Central (now Central Union) Trust Company of New York, Trustee, dated January 5, 1897 (hereinafter called the General Mortgage). The General Mortgage Bonds mature January 5, 1997, bear interest at 4%, and are the joint obligations of the two companies. They are not subject to redemption before maturity. Bonds to the amount of $96,524,000 (including $2,831,000 in the Treasury) were outstanding December 31, 1919, and on December 31, 1920, there were outstanding $95,980,000 of which $2,711,000 were in the Treasury of the Holding Company. The properties mortgaged and pledged under the General Mortgage include the properties of the Reading Coal Company, the railroad equipment and certain real estate owned by the Holding Company, all the stock of the Reading Coal Company and of the Reading Railway Company, and certain bonds of the Railway Company. (Record, pp. 157, 158.)

The Holding Company had also issued and outstanding equipment trust obligations and other bonds, its total funded debt on December 31, 1920, amounting to $132,356,015.28 (Record, p. 200).

The Original Plan

Pursuant to the interlocutory decree of the District Court, the following plan was filed on February 14, 1921 (Record, pp. 40-45):

> **"1. The Reading Company will assume the $96,524,000 General Mortgage 4% bonds, which are a joint obligation of the Reading Company and The Philadelphia & Reading Coal & Iron Company (hereinafter called the Coal Company), and will agree to save the Coal Company and its property harmless therefrom.**

"2. The Coal Company will pay to the Reading Company $10,000,000 in cash, or current assets at market value, and $25,000,000 in 4% mortgage bonds of the Coal Company. The mortgage under which they are to be issued may contain provision for the issue thereunder of additional bonds to provide for additions, betterments and improvements to a limited amount, to be determined by the Reading Company and the Coal Company prior to the creation of the mortgage, and shall contain provision for a proper sinking fund for the retirement of bonds issued thereunder. The $25,000,000 bonds issued by the Coal Company to the Reading Company shall mature on January 1, 1997, the same date as the General Mortgage bonds. The bonds issued by the Coal Company shall be subject to redemption at par and accrued interest on any semi-annual interest date as a whole but not in part, except out of the moneys in the sinking fund.

"3. Except as otherwise herein expressly provided, general releases of all claims and liabilities as between the Reading Company and the Coal Company, including the claim of approximately $70,000,000 carried on the books of the Reading Company as an asset and on the books of the Coal Company as a liability, will be exchanged.

"4. The Reading Company will agree that it will obtain the release of the coal property from the lien of the General Mortgage and the discharge of the Coal Company from liability on the General Mortgage bonds, provided such release and discharge can be secured by payment by the Reading Company to the bondholders of a premium not exceeding 10% upon the par value of the outstanding General Mortgage bonds. Such release and payment will be made from time to time as the acquiescence of the several bondholders shall be given. The Reading Company will make payment of said premium on the order of the committee to be formed in the interest of the bondholders. Said committee will call for the deposit of bonds and will be authorized by the depositors to return to them their bonds stamped as assenting to the release and dis-

charge above mentioned, or to return to them, in the discretion of the committee, refunding and improvement mortgage bonds of the Reading Company hereinafter described for an equal principal amount and bearing 4% interest. Though the committee will order payment of the premium from time to time as the bonds are deposited, it will, in the first instance, cause to be issued depository receipts for the General Mortgage bonds and will retain the General Mortgage bonds until it shall have determined that a sufficient percentage of bonds has been deposited to declare in effect the plan of exchange for refunding and improvement mortgage bonds, or that in its judgment it is improbable that a sufficient amount of bonds will be so deposited. Upon such determination it shall deliver to the holders of the depository receipts the refunding and improvement mortgage bonds or General Mortgage bonds stamped as aforesaid, as the case may be. The depository will collect and pay out the interest on the deposited bonds pending the determination of the committee as aforesaid.

"5. It is assumed that the Attorney General will ask the Court to direct the release of the stock of the Coal Company from the lien of the General Mortgage on such terms as the Court may fix. If practicable the Coal Company will consolidate with Delaware Coal Company, of which it owns the entire capital stock, and the consolidated company will issue stock without par value to the Reading Company. If that is not practicable, a new corporation will be created to acquire from the Reading Company the stock of the Coal Company, or the interest of the Reading Company therein, and such new corporation will issue no par value stock. The number of shares to be issued of the consolidated Coal Company or of such new corporation may be 1,400,000.

Such no par value stock will be sold to the stockholders of the Reading Company, preferred and common, share and share alike, for $5,600,000, or $2.00 for each share of Reading Stock. It is proposed to carry out this sale, in accordance with

the precedent established by the Union Pacific-Southern Pacific case, by distributing to Reading stockholders assignable certificates of interest in the Coal Company stock exchangeable for such stock only when accompanied by an affidavit that the holder is not the owner of any stock of Reading Company. Any further steps, which may be deemed necessary by the Court, will be taken to the end that an independent board and management to be approved by it will be maintained for the Coal Company, so that the independence of this company need not await the necessarily gradual process of the distribution of the stock of the Coal Company among persons not holders of stock in the Reading Company.

"6. The Reading Company will merge the Philadelphia & Reading Railway Company under the authority contained in the present charter of the Reading Company, and will subject the Railway property to the direct lien of the General Mortgage. The name of the Reading Company, after merger, will not be changed. The Reading Company will accept the Pennsylvania Constitution of 1874, and it will proceed under the Act of 1856 to surrender those of its powers which are inappropriate for a railroad corporation of Pennsylvania. Thus the Reading Company will be in all respects subject to the regulation of State and Federal authorities as a common carrier, and the relation of the Reading Company, as a specially chartered holding company, to the Philadelphia and Reading Railway Company will be terminated.

"7. If and whenever the General Mortgage bondholders' committee shall determine to declare the plan of exchange effective, the Reading Company shall execute a refunding and improvement mortgage, which shall constitute a direct lien upon all the railroads, railroad property, railroad equipment and railroad stocks and bonds then owned by the Reading Company or thereafter acquired by means of bonds issued thereunder. Deposited General Mortgage bonds will be kept alive under said re-

funding and improvement mortgage until the General Mortgage is released. The refunding and improvement mortgage will contain appropriate provision for the reservation of bonds to refund outstanding General Mortgage bonds and other prior lien bonds or obligations. It will be an open mortgage in modern form with appropriate provision for the issue of additional bonds for the acquisition of new property and for additions, betterments and improvements to the mortgaged property.

"8. The Court will be asked to defer the actual sale of the stock held by the Reading Company in the Central Railroad of New Jersey pending the grouping of railroads by the Interstate Commerce Commission under the Transportation Act, but subject to the further order of the Court. It is assumed that the Attorney General will ask the Court to make an order assuring the voting of the stock pending such sale in the manner approved by the Court. A detailed plan for the prompt disposition of the stock of the Lehigh and Wilkes-Barre Coal Company by the Central Railroad of New Jersey has been submitted separately."

Proceedings in the District Court

The Original Plan, having been prepared in consultation with counsel for the Government, and after consultation from time to time with the District Court (Record, p. 278), was approved by the then Attorney General of the United States, except as to the disposition to be made of the stock of the Central Railroad Company (Record, p. 45).

The District Court ordered that the Original Plan and the suggestions of the United States relating thereto be served upon the Central Union Trust Company of New York, Trustee under the General Mortgage, and be open to the inspection of all stockholders; and set March 1, 1921, for a further hearing on the proposed Plan (Record, p. 46).

On March 1, 1921, a supplemental bill was filed by the United States to make the Central Union Trust Company of New York, as Trustee under the General Mortgage, a party to this cause (Record, p. 48).

On March 15, 1921, petitions for leave to intervene were filed by or on behalf of numerous stockholders and by holders of $3,056,000 General Mortgage Bonds pursuant to oral order of the Court at the hearing on March 1, 1921 (Record, pp. 51-148).

The Insurance Companies, appellants (in addition to the objection to the participation of the preferred stockholders in the coal rights which is the basis of their appeals), objected to the provisions of paragraphs 4 and 5 of the Original Plan, which contemplated the ultimate release of the coal property and the immediate release of the stock of the Reading Coal Company from the lien of the General Mortgage and the payment of not to exceed $9,400,000 to the bondholders for the release of the property (Record, pp. 70-76).

The Central Union Trust Company of New York, as Trustee under the General Mortgage, filed an answer in which, among other things, it alleged that it was not necessary that the General Mortgage, or the lien thereof, should in any wise be disturbed in order fully to carry out and comply with the Mandate of this Court, and that in this action the Court was without power to disturb the same (Record, pp. 150-152).

By orders filed April 12, 1921 (Record, pp. 203-207), the District Court granted leave to petitioning stockholders and General Mortgage bondholders to intervene, directed that the Central Union Trust Company of New York, Trustee, be made a party defendant and set down for argument on May 2, 1921, the following questions (Record, p. 206):

> "(1) (a) Whether the sale provided for in paragraph Five of the Reading Plan is such a disposition of the interest of Reading Company in the

stock of The Philadelphia & Reading Coal & Iron Company as accomplishes the express purpose of the mandate of the Supreme Court of the United States requiring disposition by Reading Company of such stock because the holding of it has been and would be unlawful; (b) and if the mandate is thereby complied with, whether such disposition confers upon any one class of stockholders of Reading Company any benefit to the prejudice of the legal rights of any other class of stockholders.

"(2) Whether the stock of the Coal Company should be sold free from the lien of the General Mortgage, or whether a sale of Certificates of Interest therein would be a compliance with the provisions aforesaid of the mandate of the Supreme Court of the United States.

"(3) Whether the Reading Company should offer a premium of ten per cent. to the General Mortgage bondholders for release of the Coal Company's property from the lien of the mortgage, or whether the requirements of the mandate of the Supreme Court of the United States may be fulfilled by proper injunctive provisions in the decree to be entered in this cause."

Modifications of the Original Plan

At the hearing on May 2, 1921, the Holding Company, with the approval of the Attorney-General of the United States, submitted, in open court, modifications of the Original Plan, which met the objections of the bondholders and the Trustee under the General Mortgage (Record, p. 290). Such modifications were thereafter, in pursuance of the direction of the District Court at the hearing on May 2, 1921, reduced to writing by the Holding Company and the Attorney-General of the United States and filed in the District Court on May 12, 1921. (Record, pp. 210, 290.)

The effect of the Modifications was, briefly, to eliminate (1) the provision of paragraph 4 of the Original Plan looking towards the release of the coal property in con-

sideration of a premium of 10% payable to General Mortgage Bondholders, and (2) the provision of paragraph 5 of the Original Plan for the immediate release of the stock of the Reading Coal Company from the General Mortgage.

The modifications filed are as follows (Record, p. 210):

"Paragraph numbered 4 of the Plan as modified will read as follows:

"4. The Reading Company will agree with the Coal Company that, at or before the maturity of the General Mortgage bonds, it will obtain the release of the Coal Company's property from the lien of the General Mortgage and the discharge of the Coal Company from liability on the General Mortgage bonds.

"Paragraph numbered 5 of the Plan as modified will read as follows:

"5. If the Court so orders, the Reading Company will, subject to the lien of the General Mortgage, sell, assign and transfer all its right, title and interest in and to the stock of the Coal Company, including the present right to vote and receive dividends thereon, to a new corporation to be formed with appropriate powers, and will agree to save the new corporation and said stock harmless from the lien of the General Mortgage, and will agree to obtain, at or before the maturity of the General Mortgage, the release of the stock of the Coal Company from the lien of the General Mortgage and the assignment, transfer and delivery of said stock to the new corporation—all in consideration of the payment by the new corporation to the Reading Company of the sum of $5,600,000 and its agreement to issue its shares to the stockholders of the Reading Company as hereinafter provided.

"The new corporation will issue 1,400,000 shares of stock without par value. Such no par value stock will be sold by the new corporation to the stockholders of the Reading Company, preferred and common, share and share alike, for $5,600,000, or $2.00 for each share of Reading stock. Provi-

sion will be made for the disposition by the Reading Company of any rights to subscribe which may not be availed of by the Reading stockholders within such period as may be fixed by the Court, to the end that the new corporation shall receive the full purchase price of $5,600,000. It is proposed to carry out this sale in accordance with the precedent established by the Union Pacific-Southern Pacific case, by issuing to Reading stockholders, with or without the intervention of a trustee, as may be provided for in the final decree of the Court, assignable certificates of interest in the stock of the new corporation exchangeable for such stock only when accompanied by an affidavit that the holder is not the owner of any stock of the Reading Company.

"In addition there will be embodied in the final decree a permanent injunction against the new corporation exercising its voting power on the stock of the Coal Company in such a way as to bring about any new relations between the Coal Company and the Reading Company of the character complained of in the present suit. Any further steps, which may be deemed necessary by the Court, will be taken to the end that an independent board and management to be approved by it will be maintained for the Coal Company, so that the independence of this Company need not await the necessarily gradual process of the distribution of the no par value stock of the new corporation among persons not holders of stock in the Reading Company.

"The final decree may provide that if by reason of default on the General Mortgage bonds the Trustee, the Central Union Trust Company, shall exercise the right to vote the stock of Reading Coal Company, it shall so exercise that right as not to bring about unity of management between said Coal Company and Reading Company; and the final decree may further provide that, in the event the Trustee at any time is obliged to sell the stock or properties of Reading Coal Company, it shall dispose of such stock and properties separately from the properties of Reading Company and to different interests.

"Paragraph numbered 7 of the Plan will be omitted. Paragraph numbered 8 of the Plan will be numbered 7."

The Modified Plan, having been prepared in consultation with counsel for the Government, and after consultation from time to time with the District Court (Record, p. 278) was approved by the present Attorney General of the United States, except as to the disposition to be made of the stock of the Central Railroad Company (Record, p. 277).

The Final Decree of the District Court

On May 21, 1921, the District Court (Buffington, Davis and Thompson, JJ., sitting under the Expediting Act so-called) rendered an opinion unanimously approving the Modified Plan (Record, pp. 278-286), and on June 6, 1921, entered a Final Decree in accordance with that opinion (Record, pp. 287-312).

Summary of the Modified Plan

The Modified Plan as supplemented by the Final Decree may be summarized as follows:

(a) *The relation between the Holding Company and the Reading Coal Company.* The Holding Company will assume the $96,524,000 General Mortgage 4% Bonds ($93,269,000 after deducting bonds in the Treasury) which are the joint obligation of the Holding Company and the Reading Coal Company, and will agree to save the Reading Coal Company and its property harmless therefrom. The Holding Company will receive from the Reading Coal Company $10,000,000 in cash or cash assets and $25,000,000 in 4% Mortgage Bonds of the Reading Coal Company, and will exchange general releases with the Reading Coal Company (Record, p. 274). The Holding Company owns all the stock (par value $8,000,000) of the Reading Coal

Company, subject to the lien of the General Mortgage (Record, p. 157). The Holding Company will, subject to the lien of the General Mortgage, sell its interest in the stock of the Reading Coal Company, including the present right to vote and receive dividends thereon, to the New Coal Company (a new corporation created by the Court's order, of which the Court will retain control so as to prevent its being used to thwart the decree), for $5,600,000, and the New Coal Company's agreement to issue its shares as follows (Record, pp. 275, 284). The stock of the New Coal Company (1,400,000 shares without par value) will be issued to a trustee or trustees appointed by the District Court, who will issue assignable certificates of interest in the stock of the New Coal Company, exchangeable for such stock only when accompanied by an affidavit stating among other things that the holder is not the owner of any stock of the Holding Company. These certificates of interest will be offered for sale to the stockholders of the Holding Company, preferred and common, share and share alike, for $5,600,000 or $2 for each share of stock of the Holding Company (Record, p. 275). Stockholders of the Holding Company cannot, however, continue stockholders of the Holding Company and become stockholders of the New Coal Company during the conversion period (Record, pp. 295, 302-308).

(b) *The relation between the Holding Company and the Reading Railway Company.* The Holding Company owns all the stock (par value $42,481,700) and $20,000,000 bonds of the Reading Railway Company, subject to the lien of the General Mortgage (Record, p. 157). The Holding Company will merge the Reading Railway Company and will subject the railway property to the direct lien of the General Mortgage, will accept the Pennsylvania Constitution of 1874 and proceed under the Pennsylvania Act of 1856 to surrender those of its powers which are inappropriate for a railroad corporation of Pennsylvania.

The resulting company, the New Railway Company, will be in all respects subject to the regulation of State and Federal authorities as a common carrier (Record, pp. 276-277).

(c) *The relation between the Holding Company and the Central Railroad Company.* The Holding Company owned stock of the Central Railroad Company to the par amount of $14,504,000, constituting more than a majority of its stock, subject to the pledge thereof under the Jersey Central Collateral Trust Mortgage securing bonds to the amount of $23,000,000 (Record, p. 158). The Holding Company was directed to transfer to Trustees appointed by the District Court, subject to the lien of the Jersey Central Collateral Trust Mortgage, its right, title and interest in the stock of the Central Railroad Company; the final disposition of said stock to be deferred, in view of the possible groupings of railroads by the Interstate Commerce Commission under the Transportation Act of 1920 (41 Stat. 456, 480), until ordered by said Court (Record, pp. 277, 296-297).

(d) *The relation between the Central Railroad Company and the Wilkes-Barre Coal Company.* The Central Railroad Company was directed to dispose of all the capital stock of the Wilkes-Barre Coal Company owned by it to persons or corporations who are not its own stockholders, or stockholders of either the Holding Company, the Reading Railway Company or the Reading Coal Company, and who previous to or at the time of the purchase shall qualify as purchasers by a duly executed affidavit in one of the forms annexed to the decree (Record, p. 298).

The Appeals from the Final Decree of the District Court

On June 16, 1921, the Insurance Companies and on August 3, 1921, the Prosser Committee, both being or representing intervening common stockholders, appealed from the decree approving the Plan. The Prosser Committee

represents 407,728 shares of common stock of the Holding Company (Record, p. 208), which is less than thirty per cent. of the total common stock (1,400,000 shares) and less than fifteen per cent. of the entire capital stock (2,800,000 shares) of the Holding Company. The Insurance Companies own 8,400 shares of common stock of the Holding Company (Record, p. 208), which is six-tenths of one per cent. of the common stock and three-tenths of one per cent. of the entire capital stock of the Holding Company. The assignments of error are set out in the Record, pages 317-320 and 333-337. The appellants contend that the right to subscribe for the certificates of interest in the stock of the New Coal Company, described in paragraph (a) of the above Summary of the Modified Plan (paragraph five of the Plan —Record, p. 275) belongs to the common stockholders of the Holding Company, and to them alone to the exclusion of preferred stockholders. The Holding Company believes that the right to subscribe was properly accorded to all stockholders, share and share alike. This is the only issue presented by these appeals.

The Order for Reargument

These appeals were argued before this Court January 16, 1922, and thereafter on February 27, 1922, the following order of this Court was entered:

> "IT IS ORDERED BY THE COURT that these cases be restored to the docket for reargument and assigned for hearing as the first cases for April 10th next, on the question whether the decree in the District Court, in which these are appeals, is in conformity with the opinion of this Court in *United States* v. *Reading Company*, 253 U. S. 26, and that the Attorney General be advised of this order."

Under date of March 14, 1922, following a request of counsel, the Clerk of this Court notified counsel that the Court desires special attention to be given in the reargument to the following questions:

"1. Whether the disposition by the Reading Company of the stock of the Philadelphia & Reading Coal & Iron Company, contemplated and ordered in the decree of the District Court, will establish such entire independence between the Reading Company, present and prospective, and the Philadelphia & Reading Coal & Iron Company and the new company to be organized, as is required by the opinion and judgment of this Court.

"2. Whether the general mortgage having been executed, and the bonds secured by it issued, as a part of the process of forming the combination held to be unlawful, there is any legal or practical difficulty in providing, by appropriate modification of the decree, for sale of the Coal Company's stock, owned by the Reading Company, free from the lien of that mortgage, and from the lien of the contemplated new mortgage.

"3. Whether compliance with the decree will confer on any one class of stockholders of the Reading Company any benefit to the prejudice of the rights of any other class of stockholders.

"4. What the basis is upon which the amount and character of the payments to be made by the Coal Company and by the new Company to the Reading Company was arrived at, and what the reasons are for adopting it."

ARGUMENT

I

The decree of the District Court is in conformity with the opinion of this Court in *United States* v. *Reading Company*, 253 U. S. 26.

This Court directed that the combination of the Holding Company, the Reading Railway Company, the Reading Coal Company, the Central Railroad Company and the Wilkes-Barre Coal Company, existing and maintained through the Holding Company, be dissolved. It directed that such provision be made for the disposition of the shares of stock and bonds and other property of the various companies held by the Holding Company as might be necessary to establish the entire independence from that Company and from each other of the Reading Railway Company, the Reading Coal Company, the Central Railroad Company, and the Wilkes-Barre Coal Company. It directed that such disposition be made of the stocks and bonds of the Wilkes-Barre Coal Company held by the Central Railroad Company as might be necessary to establish entire independence between these two companies. It directed that all these things be done, to the end that the affairs of all of these now combined companies might be conducted in harmony with the law. (253 U. S. 64).

The combination to be dissolved is one "existing and maintained through the Holding Company." This combination existed and was maintained by the Holding Company by ownership of the entire capital stock of the Reading Railway Company, of the entire capital stock of the Reading Coal Company, of more than a majority of the capital stock of the Central Railroad Company, and by the latter's ownership of more than ninety per cent. of the stock of the Wilkes-Barre Coal Company.

The decree of the District Court does dissolve the unlawful combination so existing and maintained. It does contain provision for such disposition of the shares of

stock and bonds and other property of the various companies held by the Holding Company and of the Wilkes-Barre Company held by the Central Railroad Company as is necessary to establish their entire independence from the Holding Company and from each other.

The decree of the District Court goes further than that. Not content with establishing independence between these combined companies it undertakes, so far as the basic combination of the Reading Railway Company and the Reading Coal Company is concerned, not merely to establish independence, but to perpetuate it by vesting control of the Reading Coal Company in the New Coal Company, a creature of the Court.

II

The disposition by the Holding Company of the stock of the Reading Coal Company, contemplated and ordered in the decree of the District Court, will establish such entire independence between the Holding Company and the New Railway Company, on the one hand, and the Reading Coal Company and the New Coal Company, on the other, as is required by the opinion and judgment of this Court.

The decree disposes of the Holding Company's equity in the stock of the Reading Coal Company to a New Coal Company, the creature of the Court; and disposes of the stock of the New Coal Company to persons not themselves owners of stock in the Holding Company.

The final decree of the District Court provides (Record, p. 292):

> "*c.* The stock of the new corporation [the New Coal Company] shall be issued to a Trustee or Trustees appointed by the Court. Such Trustee or Trustees shall issue certificates of interest therein as contemplated by the Modified Plan and as hereinafter provided. The Reading Company [the

Holding Company] shall offer such certificates of interest for subscription to its stockholders, preferred and common, share and share alike, and may issue to them assignable warrants evidencing their right to subscribe for said certificates of interest. Neither the defendant Reading Company nor any corporation controlled by it nor any person acting in its interest shall acquire by purchase or otherwise any of said certificates of interest. Such certificates of interest shall be delivered to the subscribers therefor upon payment in full of the subscription price and compliance in all respects with the terms prescribed in the offer. All such certificates shall be registered by the Trustee or Trustees in the names of the purchasers. They shall be substantially in the form hereto annexed marked "Form A." [Record, p. 302.]

"*d.* The Trustee or Trustees shall be entitled and it shall be their duty, to vote or issue proxies for voting in respect of any and all of said shares of the new corporation held by the said Trustee or Trustees unless otherwise hereafter directed by this Court.

"*e.* The Trustee or Trustees shall collect and receive any and all cash dividends paid on the stock of the new corporation held by the Trustee or Trustees. Upon the exchange, as hereinafter set forth, of any certificate of interest for shares of capital stock of the new corporation held by the Trustee or Trustees, the Trustee or Trustees shall pay in cash to the owner of the certificate of interest so exchanged or upon his order the amount of all cash dividends collected by the Trustee or Trustees, in respect of the number of shares represented by such certificate of interest, but without interest thereon, and shall execute and deliver to such owner or upon his order a dividend order or assignment for the amount of any dividends declared but not then payable in respect of shares vested at the time of such exchange in the Trustee or Trustees as the registered stockholder entitled thereto. Any interest realized or allowed by the Trustee or Trustees upon funds paid to the Trustee or Trustees as dividends shall be applicable to the payment of the compensation of the Trustee or

Trustees and the expenses of the administration of the trust, and any balance thereof remaining shall be paid to the defendant Reading Company unless otherwise ordered by the Court.

"All dividends payable otherwise than in cash which shall be declared by the new corporation shall be received and held by the Trustee or Trustees for the *pro-rata* benefit of said registered owners, from time to time, of the certificates of interest, upon the same terms and conditions as the shares originally deposited, and shall be distributed to the persons who shall be the respective owners of the certificates of interest when and as and only when and as, the shares originally deposited are distributed to them respectively, subject to any necessary adjustment by scrip or otherwise, in the discretion of the Trustee or Trustees, in respect of fractional shares.

"No deduction shall be made by the Trustee or Trustees in the distribution of such dividends or subscription rights for any commissions or expenses of the Trustee or other costs of collection or payment.

"*f.* Upon surrender of any outstanding certificates of interest by the registered owner thereof or his assignee, the Trustee or Trustees shall deliver to him stock certificates for the number of shares of the new corporation represented by the surrendered certificate of interest, which stock certificates shall be issued by the new corporation and registered on its books in the name of the new holder, upon condition, however, that the applicant for such exchange shall file with the Trustee a duly executed affidavit in one of the forms hereto annexed."

The form of affidavit for use by individuals is as follows (Record, p. 305):

"STATE OF ..... COUNTY OF....., ss.:

....., being duly sworn, deposes and says:

That deponent is a *bona fide* owner in his (or her) proper right of a certificate or certificates of interest numbered for shares registered

in the name of issued by as Trustee, under a decree entered on the day of June, 1921, by the District Court of the United States for the Eastern District of Pennsylvania, in the suit of the United States of America against Reading Company and others, and makes this affidavit for the purpose of procuring the issue of shares of the capital stock of the Company held by said Trustee, in exchange for said certificate (or certificates) of interest. That deponent does not own in his (or her) own right any shares of the capital stock of the Reading Company, a corporation of the Commonwealth of Pennsylvania, whether registered in his (or her) own name on the books of said Reading Company or registered in the names of others for deponent's use and benefit. That deponent, in making this application, is not acting for or on behalf of any stockholder of the Reading Company, or in concert, agreement, or understanding with any other person, firm or corporation for the control of the Company in the interest of the Reading Company, but in his (or her) own behalf in good faith.

Sworn to before me this }
day of , 1921. }

Appropriate variations are made in the forms for use by corporations, partnerships and trustees (Record, pp. 306-308).

Under these provisions the stockholders of the Holding Company, unless they choose to sell their stock in the Holding Company instead, are merely a conduit for the sale of the stock of the New Coal Company to others. The control of the New Coal Company, and hence of the Reading Coal Company, is immediately vested in trustees appointed by the District Court, and does not pass from them until the certificates of interest which the trustees will issue shall have become the property of persons not owners of stock in the Holding Company. Holders of

certificates of interest will be under pressure to sell them or their stock in the Holding Company, because they cannot collect dividends, or vote, on the stock of the New Coal Company, until they do. The Decree further contains the following provisions for keeping watch of the process of conversion of certificates of interest into stock of the New Coal Company and, if it is unduly retarded, bringing the matter to an end by directing a forced sale (Record, pp. 294, 295):

> "*g.* The amount of certificates of interest surrendered for exchange shall be reported monthly by the Trustee or Trustees to the Attorney General of the United States, and at any time upon the request of the Attorney General of the United States the Trustee or Trustees shall furnish him with any additional information which he may require relating to the carrying out of this decree.
>
> "*h.* If, at any time after July 1, 1924, any of such certificates of interest shall remain outstanding, the Court, in its discretion, after a hearing, upon such notice to holders of certificates of interest as it may direct, may order the shares of the new corporation, represented by said certificates, to be sold and the proceeds distributed to the registered owners of such certificates."

The provisions with respect to the disposition of the stock of the Reading Coal Company fully conform to the precedent established in the Union Pacific-Southern Pacific case. In that case this Court decided that the combination of the Union Pacific Railroad Company and the Southern Pacific Company, through the ownership by Union Pacific of 46% of the capital stock of Southern Pacific, violated the Anti-Trust Act, in view of the fact that the lines of railroad of these two companies were normally competing. *United States* v. *Union Pacific Railroad Company,* 226 U. S. 61. Thereafter, this Court was asked by the Attorney General and counsel for the Union Pacific Railroad Company

"to instruct the United States District Court for the District of Utah, by a provision incorporated in the mandate of this Court when issued or otherwise, whether or not a sale of the Southern Pacific Company shares held by said appellees, to the shareholders of the appellee Union Pacific Railroad Company, substantially in proportion to their respective holdings, or a distribution thereof by dividend to the Union Pacific stockholders entitled to such dividend, would, in the opinion of this Court, constitute a disposition of said shares in compliance with the opinion herein filed on December 2, 1912."

This Court decided that such disposition would

"perpetuate the domination and control of the Union Pacific over the Southern Pacific Company because of the power given to the Union Pacific Company's stockholders to choose the directors of the Southern Pacific Company." *United States* v. *Union Pacific Railroad Company,* 226 U. S. 470, 475."

In conformity with that opinion the District Court for the District of Utah by its decree ordered (see "Decrees and Judgments in Federal Anti-Trust Cases," compiled by Roger Shale under direction of G. Carroll Todd, p. 217, Government Printing Office, 1918):

"*Section 4.* The shares of the defendant Southern Pacific Company held by the defendant Oregon Short Line Railroad Company remaining after the sale to the Pennsylvania Railroad Company of 382,924 shares thereof as hereinabove provided, to wit, 883,576 shares, or the entire holdings if such sale to the Pennsylvania Railroad Company shall not be consummated within 30 days from the date hereof, shall be transferred forthwith to the Trustee and registered in its name on the books of the Southern Pacific Company, and certificates therefor delivered to the Trustee.

* * * * * * *

"*Section 5.* Prior to November 1, 1913, the defendants Union Pacific Railroad Company and

Oregon Short Line Railroad Company shall offer to all stockholders of the former, common and preferred (registered as such on a date to be designated in the offer and not more than 40 days from its date) or to their assignees, the right to subscribe for certificates of interest representing the said Southern Pacific Company shares transferred to the Trustee as provided hereunder, substantially in the proportion of their respective holdings, with such allowance in fixing the distribution ratio as the above-named defendants may deem necessary for possible conversions of convertible bonds of the said Union Pacific Railroad Company. The offering shall include all accumulated dividends appertaining to said shares, and shall be at such price and upon such other terms as the defendants Union Pacific Railroad Company and Oregon Short Line Railroad Company shall determine, except as specifically herein prescribed or as otherwise directed by the court by a subsequent order or decree.

* * * * * * *

"*Section 6.* The Trustee shall execute and issue certificates of interest representing the shares transferred to it hereunder and shall deliver them at its office in the City of New York to the subscribers therefor under section 5 hereof, upon payment in full of the subscription price and compliance in all respects with the terms prescribed by the offering, or by any subscription receipt issued under section 7 hereof, to be performed by the subscribers to entitle them to receive such certificates of interest; and in like manner shall deliver such certificates of interest upon full payment therefor to any other purchasers to whom the defendants Union Pacific Railroad Company and Oregon Short Line Railroad Company shall be authorized by the court to sell the same. All such certificates shall be registered by the Trustee in the names of the purchasers. They shall be substantially in the form hereto annexed marked "Form A."

* * * * * * *

"*Section 11.* At any time upon demand, at its office in the city of New York, upon surrender of

any outstanding certificate of interest by the registered owner thereof or his assignee, the Trustee shall deliver to him stock certificates for the number of shares of the defendant Southern Pacific Company (of the par value of $100 each) represented by the surrendered certificate of interest, which stock certificates shall be issued by the said Southern Pacific Company and registered on its books in the name of the new holder, upon condition, however, that the applicant for such conversion or exchange shall file with the Trustee a duly executed affidavit in one of the forms hereto annexed."

The affidavit attached to the decree in the Union Pacific-Southern Pacific case (which is substantially in accordance with the affidavit required by the decree of the District Court in this case) is as follows:

"State of , County of :

being duly sworn deposes and says:

That deponent is the *bona fide* owner in his own proper right of a certificate or certificates of interest numbered for shares registered in the name of , issued by the Central Trust Company, of New York, as Trustee, under a decree entered on the day of June, 1913, by the District Court of the United States for the District of Utah, in the suit of the United States of America against Union Pacific Railroad Company and others, and makes this affidavit for the purpose of procuring the issue of shares of the capital stock of the Southern Pacific Company held by the said Trustee, in exchange for said certificate (or certificates) of interest. That deponent does not own in his (or her) own right any shares of the capital stock of the Union Pacific Railroad Company, a corporation of the State of Utah, whether registered in his (or her) own name on the books of said Union Pacific Railroad Company or registered in the names of others for deponent's use and benefit. That deponent, in making this application, is not acting for or on behalf of any

> stockholder of the Union Pacific Railroad Company, or in concert, agreement, or understanding with any other person, firm, or corporation for the control of the Southern Pacific Company in the interest of the Union Pacific Railroad Company, but in his own behalf in good faith.
>
> Sworn to before me this day of , 191 ."

In two respects the provisions of the decree for the disposition of the stock of the Reading Coal Company go further than the decree in the Union Pacific case:

(1) The intervention of the New Coal Company between the Reading Coal Company and the ultimate beneficial ownership to be established pursuant to the decree, furnishes an additional safeguard. The names of the officers and directors of the New Coal Company to be elected and appointed in the first instance must be submitted to the District Court for its approval. (Record, p. 291). The decree provides:

> "*a.* The names of the officers and directors of the new corporation [the New Coal Company] to be elected and appointed in the first instance shall be submitted to the Court for its approval, and no officer or director of the new corporation shall be an officer or director of the Reading Company."

The New Coal Company is required by the Court to enter its appearance in this cause and thereby submit itself to the jurisdiction of the District Court for all the purposes of this cause. (Record, p. 291.) The decree provides:

> "*b.* The Reading Company shall not sell, assign or transfer its right, title and interest in the stock of the [Reading] Coal Company to the new corporation [the New Coal Company] unless and until the new corporation shall enter its appearance herein by counsel and thereby submit itself to the jurisdiction of this Court for all purposes of this cause; and it shall thereupon become a party defend-

ant in this cause and subject to the provisions of this decree. * * * "

The New Coal Company and its officers and directors, are thereupon enjoined and restrained from exercising the voting power on the stock of the Reading Coal Company so as to form such a combination between the Reading Coal Company and the Reading Company (*i. e.* the Holding Company or the New Railway Company) as has been adjudged unlawful in this cause (Record, p. 295). The decree provides:

> "*j.* Effective upon its becoming a party defendant in this cause, as hereinbefore provided, the new corporation, its officers and directors are hereby enjoined and restrained from exercising the voting power on the stock of the Coal Company so as to form such a combination between the Coal Company and the defendant Reading Company as has been adjudged unlawful in this cause."

Thus the District Court has created a situation which very effectively perpetuates the dissolution decree.

The District Court will retain control of the New Coal Company so as to prevent its being used to thwart the decree. The District Court said in its opinion (Record, pp. 283, 284):

> "* * * In the creation of such a corporation by this Court's order, we follow a general course pursued in the case of United States v. Du Pont, *et al.*, 188 F. R., 127, and the wisdom of so doing will be seen by an examination of the opinion lately filed in that case, where the purpose of such procedure is fully explained. By the creation of this new corporation by the directions of this Court and by its retention of jurisdiction to enforce this decree as therein provided, the Court can, if such contingency should arise, by its control of this newly formed corporation, control all of its stockholders and prevent such stock from ever being used to thwart the decree made in pursuance of the plan."

The opinion lately filed, above referred to, in *United States* v. *E. I. du Pont de Nemours & Company,* is reported in 273 Fed. Rep., 869.

(2) The decree of the District Court goes further than did the decree in the Union Pacific-Southern Pacific case also in that the Reading decree provides (Record, p. 295) that, during the period allowed for the conversion of certificates of interest into stock of the New Coal Company, no present stockholder of the Holding Company shall be a purchaser of stock of the New Coal Company if still a stockholder of the Holding Company. This provision relates to the beneficial ownership and not to holdings as broker, pledgee, trustee, agent or otherwise in a representative capacity. The decree provides:

> "*i.* During the period allowed for the conversion of the certificates of interest into stock of the new corporation [the New Coal Company], no present stockholder of the Reading Company shall be a purchaser of stock of the new corporation if still a stockholder of the Reading Company; and the Attorney General of the United States shall have access to the stock transfer books of the Reading Company and the new corporation for the purpose of enabling him to enforce compliance by such stockholders with this provision of this decree; but nothing herein contained shall extend to holdings as broker, pledgee, trustee, agent or otherwise in a representative capacity."

It was intended by this provision to prevent the evasion of the decree by the sale of certificates of interest in the market and the purchase of stock of the New Coal Company in the market by stockholders of the Holding Company.

Finally the decree provides (Record, p. 295):

> "*k.* The Reading Company, and all persons acting for or in its interest, are hereby perpetually enjoined from acquiring, receiving, holding, voting,

or in any manner acting as the owner of any of the shares of the capital stock of the new corporation; and the new corporation, and all persons acting for or in its interest, are hereby perpetually enjoined from acquiring, receiving, holding, voting, or in any manner acting as the owner of any of the shares of the capital stock of the Reading Company."

III

The fact that the General Mortgage Bonds remain outstanding and the General Mortgage remains a lien on the property and stock of the Reading Coal Company as well as on the property of the New Railway Company is not inconsistent with the entire independence of the Reading Coal Company from the Holding Company and the New Railway Company.

The General Mortgage constitutes, and under the Modified Plan and decree will continue, a lien, among other things, upon the stock and property of the Reading Coal Company. Section 4 of the Original Plan contemplated the voluntary release of the coal property from the lien of the General Mortgage and the discharge of the Reading Coal Company from liability on the General Mortgage Bonds, provided such release and discharge could be secured by payment by the Holding Company to the bondholders of a premium not exceeding ten per cent. upon the par value of the outstanding General Mortgage Bonds. Such release and payment were to be made from time to time as the acquiescence of the several bondholders was given (Record, p. 41). The acceptance of this offer was to be optional with the General Mortgage bondholders.

Section 5 of the Original Plan contemplated the release of the stock of the Reading Coal Company from the lien of the General Mortgage on such terms as the Court should fix.

These features of the Original Plan were objecte to by the Trustee under the General Mortgage an by certain bondholders and stockholders of the Holdin Company.

The General Mortgage Bonds mature January 1, 199 that is, in about 75 years. They are not subject to redem tion before maturity. The General Mortgage is printe in the Old Record, page 1653. Article Six, providing fo the release of mortgaged property, does not permit th release of the property of the Reading Coal Company a a whole, nor the release of the stock of the Reading Co Company.

Though the General Mortgage was executed and som of the bonds secured by it were issued as a part of th process of forming the combination held to be unlawfu others of the bonds (approximately one-half) secured b the General Mortgage were subsequently issued, in the o dinary course of business, for refunding, betterments, et Neither the bondholders nor the Trustee under the Ge eral Mortgage were parties to this cause until after th decision of this Court had been rendered. That decisio required "the disposition of the shares of stock and bon and other property of the various companies *held* by th Reading Company"; but it did not require that bon *issued* by the Reading Company should be disturbed.

When therefore the Trustee under the General Mo gage, and bondholders and stockholders made objection the release of the stock of the Reading Coal Company fro the lien of the General Mortgage and to the proposal f the release of the property (Record, p. 152), modificatio of the Plan were filed. (Record, p. 210) by which the obj tionable features were eliminated. The ten per cent. optio al premium to General Mortgage bondholders and the pr vision looking towards the release of the coal property fro the lien of the General Mortgage before maturity we abandoned, and it was provided that the certificates stock of the Reading Coal Company should be permitted

remain with the Trustee under the General Mortgage, though the Holding Company's right, title and interest therein and all right to receive dividends and vote thereon were to be transferred to the New Coal Company.

In the foregoing paragraphs are indicated some of the legal and practical difficulties in the way of providing for the sale of the Reading Coal Company stock owned by the Holding Company free from the lien of the General Mortgage. Enough has been said to show that very real difficulties did exist. It did not seem necessary to determine whether or not those difficulties were insuperable, for it became evident that the opinion and judgment of this Court could be fully satisfied without disturbing the lien of the General Mortgage.

It is believed that the release of the Reading Coal Company stock from the General Mortgage is neither necessary nor desirable and that the results which would be attained by such release are equally attained under the provisions of the Modified Plan and of the decree. The stock simply stands today as a muniment of title. It stands for the right to own, control and enjoy the income of the Reading Coal Company. These rights all pass under the Modified Plan and the decree to the New Coal Company.

Under the decree the Holding Company will surrender all its interest in the stock of the Reading Coal Company, including the present right to vote and receive dividends thereon, and will covenant to release said stock and the coal property from the lien of the General Mortgage at or before its maturity. The New Railway Company will be bound to save the Reading Coal Company and its property and the New Coal Company harmless therefrom (Record, pp. 274, 275). The result will be that one principal debtor will take the place of the present joint principal obligation and the Reading Coal Company and its stock and property will stand as surety for the payment of the bonds (Record, p. 188).

The value of the property subject to the General Mortgage (excluding the property and stock of the Reading Coal Company) will be so greatly in excess of the amount of outstanding General Mortgage Bonds that there is no reasonable doubt that the indemnity of the New Railway Company is ample protection for the property of the Reading Coal Company and the equity of the New Coal Company in the stock of the Reading Coal Company. Moreover, the earnings of the railroad property in the past have greatly exceeded the amount required for interest on the General Mortgage Bonds.

As of December 31, 1920, the book value of the fixed properties, which will, on the consummation of the Plan, be directly subject to the General Mortgage (excluding the stock and property of the Reading Coal Company), after deducting all liens thereon prior to the General Mortgage, was approximately $200,000,000, (Record, p. 200) or more than twice the $93,269,000 principal amount of the General Mortgage Bonds outstanding (Record, p. 157). In addition, there are pledged under the General Mortgage stocks and bonds of subsidiary railroad and terminal companies auxiliary to the lines of railroad owned by the Reading Railway Company (excluding the stock of the Reading Coal Company and the stock and bonds of Reading Railway Company) having a par value in excess of $38,000,000 (Old Record, pp. 1666-1668).

The interest on the $93,269,000 General Mortgage 4% Bonds outstanding December 31, 1920 (Record, p. 157) amounts to $3,730,760 per annum. An analysis of the statements on page 259 of the Record and of the dividend record of the Holding Company shows that the combined net earnings of the Holding Company and the Reading Railway Company, during the ten-year period 1911-1920 (excluding payments made by the Reading Coal Company to the Holding Company in the years 1911-1913, and excluding amounts in excess of $30,000,000 earned by the Reading Railway Company during that period and expended for additions and betterments to its property

after payment of taxes and all fixed charges other than interest on the General Mortgage Bonds, were more than three times the interest on the General Mortgage Bonds. In the figures referred to are included dividends paid on the Holding Company's stock in the Central Railroad Company in excess of interest on the Collateral Trust Bonds secured by that stock. It is impossible to forecast the financial outcome of the disposition of the stock of the Central Railroad Company; but, as against the possible net loss of revenue on that account, the earnings of the New Railway Company will be increased by $1,000,000 per annum which it will receive as interest on $25,000,000 of bonds of the Reading Coal Company.

In view of this substantial excess in the value of the railroad properties over the outstanding General Mortgage Bonds, and of the proved ability of the railroad properties to earn several times the General Mortgage interest requirements, it cannot be questioned that the New Coal Company and the coal properties will be placed beyond the reach of any influence or coercion by the New Railway Company, and that a default under the General Mortgage is a contingency too remote to require consideration. This remote contingency has, however, been fully guarded against by the following provision of the Final Decree (Record, p. 298):

> "6. If by reason of default on the General Mortgage bonds Central Union Trust Company of New York, the Trustee under the General Mortgage, shall exercise the right to vote the stock of the Coal Company, it shall so exercise that right as not to bring about unity of management between the Coal Company and the Reading Company; and in the event that said Trustee at any time is obliged to sell the stock or properties of the Coal Company, it shall dispose of such stock and properties separately from the properties of the Reading Company and to different interests."

IV

The issue to the Holding Company of the $25,000,000 mortgage bonds of the Reading Coal Company is not inconsistent with the entire independence of these Companies.

The $25,000,000 bonds which under the decree are to be issued by the Reading Coal Company to the New Railway Company will not enable the New Railway Company to exercise any control over the Reading Coal Company or the coal properties.

The new mortgage of the Reading Coal Company under which these bonds are to be issued will not be a lien on the stock of the Reading Coal Company, though it will be a lien upon its property.

A mortgage debt does not enable the creditor to exercise control over the debtor when the amount of the debt is safely within the debtor's ability to pay.

The balance sheet of the Reading Coal Company as of December 31, 1920 (Record, p. 198), shows a capital account of $74,471,690.53, and funded debt (after wiping out the claim of the Holding Company, as provided by the Plan) of only $870,000. Thus the fixed assets of the Reading Coal Company are practically three times the amount of the bonds to be delivered to the New Railway Company. The average annual net income of the Reading Coal Company for the five years 1916-1920, both inclusive, was $4,319,908.95 (Record, p. 199), or more than four times the interest on these bonds. Under these circumstances, the ownership of these bonds can in no way give the New Railway Company any present or prospective influence or control over the Reading Coal Company.

The $25,000,000 mortgage bonds will be a free asset in the treasury of the New Railway Company and will presumably be disposed of for cash as soon as conditions permit them to be sold upon reasonable terms.

V

What the basis is upon which the amount and character of the payments to be made by the Reading Coal Company and by the New Coal Company to the Holding Company was arrived at and what the reasons were for adopting it.

The amount and character of these payments was arrived at in an effort (1) to settle the involved financial relations between the Holding Company and the Reading Coal Company; (2) to insure to the New Railway Company and the New Coal Company, each, a sound financial structure and adequate cash working capital; (3) to limit as far as possible the requirements for new cash under difficult market conditions; and (4) to make the inevitable loss to the stockholders of the Holding Company as small as possible.

The General Mortgage Bonds, the net amount of which outstanding on December 31, 1920, was $93,269,000, are the joint obligation of the Holding Company and the Reading Coal Company. The Holding Company has a claim against the Reading Coal Company, the nominal amount of which as carried on the books of those companies as of December 31, 1920 (Record, p. 162), was $69,357,017.99. The Holding Company owns, subject to the lien of the General Mortgage, all the capital stock of the Reading Coal Company, the par amount of which is $8,000,000. These three items, the $69,357,017.99 claim, the joint obligation on $93,269,000 General Mortgage Bonds, and the $8,000,000 stockholding, were the ties to be severed.

The Reading Coal Company has only $870,000 funded debt, in addition to the General Mortgage Bonds (Record, p. 198); and its current assets are several times greater than its current liabilities. Subject only to the rights of the General Mortgage bondholders, which, as we have seen, are protected under the decree, the Holding

Company is accordingly in a position, in making the settlement with, and disposition of the stock of, the Reading Coal Company, as required by the decision of this Court, to make such arrangements as seem most advantageous to the stockholders of the Holding Company; the capital and surplus of the Holding Company itself being protected under the Plan (Record, pp. 171, 200).

Under the Plan the General Mortgage bonds are assumed by the Holding Company which will agree to save the Reading Coal Company and the New Coal Company harmless therefrom; the $69,357,017.99 claim is cancelled and general releases are exchanged between the Holding Company and the Reading Coal Company; and the Holding Company's equity in the stock of the Reading Coal Company, together with the present right to receive dividends and to vote thereon, is transferred to the New Coal Company.

The joint General Mortgage Bonds have 75 years to run and are not subject to redemption before maturity. It was obvious, however, that the character of these bonds as joint bonds must be destroyed in practical effect. This could be done by assumption of the bonds as the sole obligation of one of the companies.

The whole amount of the General Mortgage Bonds is carried on the books of the Holding Company as a liability of the Holding Company (Record, p. 200). No part of the General Mortgage Bonds is carried on the books of the Reading Coal Company as a liability of the Reading Coal Company (Record, p. 198). The General Mortage contains no indication of the liability of the companies *inter sese* except that it provides in sections 4 and 6 of Article Four (Old Record, pp. 1712, 1715) that, in case of sale in enforcement of the Mortgage, the property mortgaged thereunder shall be sold in two separate lots, of which the first lot to be sold shall be the property granted by or on behalf of the Holding Company, and the second lot to be sold shall be the property granted by or on behalf of the Reading Coal Company.

The income and assets of the New Railway Company and the Reading Coal Company have been discussed in Points III and IV. The income of the New Railway Company based on the earnings of the period from 1911 to 1920 was shown to be more than three times the interest on the General Mortgage bonds. The average income of the Reading Coal Company for the period from 1916 to 1920 did not greatly exceed that interest. Obviously as between the New Railway Company and the Reading Coal Company it was clear which must assume the General Mortgage. One or the other must take the whole load. The New Railway Company was the one which had a demonstrated capacity to carry it.

On the other hand, it was not wise that this burden should be assumed by the New Railway Company without any contribution by the Reading Coal Company. It seemed that for a proper distribution of the load the Reading Coal Company should contribute $10,000,000 in cash and cash assets and $25,000,000 in four per cent. mortgage bonds.

Had it been practicable to call the General Mortgage bonds for redemption, doubtless that would have been done and new bonds issued in about the same proportions as between the New Railway Company and the Reading Coal Company, but there were two objections, each controlling: (1) the bonds are not subject to redemption at any price; and (2) if they had been, to redeem $93,269,000 4% bonds, having 75 years to run, would, in the market conditions prevailing, have been financial madness.

Similarly had it been practicable and wise an effort might have been made to sell the $25,000,000 bonds of the Reading Coal Company immediately for cash, or, eliminating the bonds altogether, to sell the stock for a larger sum in cash. That would, however, under prevailing market conditions, have meant a grave sacrifice of the stockholders' property to provide cash for which neither Company had any immediate need.

The $10,000,000 in cash and cash assets the Reading Coal Company had to spare as appears from its tentative general balance sheet as of December 31, 1920 (Record, p. 198). The Reading Coal Company had $6,506,955.26 in Liberty Bonds and $8,245,174.27 in cash and in addition had a very large excess of current assets over current liabilities. It was thought that the Reading Coal Company could well spare $10,000,000 in Liberty Bonds and cash.

On the other hand, an examination of the comparative working assets and liabilities as of December 31, 1920, of the Holding Company, the Reading Railway Company and the New Railway Company (Record, p. 202) shows that the Holding Company had a deficit in working assets of $6,812,659.70, that the Reading Railway Company had a surplus in working assets of only $2,626,176.24 and that the New Railway Company, after giving effect to the Original Plan, would have had a surplus in working assets of only $3,843,350.51. It would seem that the resulting surplus of working assets over liabilities of $3,843,350.51 was neither inadequate nor excessive.*

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*Under the Modified Plan the cash position of the New Railway Company will be better by $9,400,000. The Original Plan contemplated (Record, pp. 162, 163) that the New Railway Company should receive in cash and cash assets.

(a) From the Reading Coal Company	$10,000,000
(b) From the Holding Company's stockholders	5,600,000
Total	$15,600,000
but should have to pay out to General Mortgage bondholders not to exceed	9,400,000
Net cash receipts	$6,200,000

All these items were taken into account in determining for working assets and liabilities of the New Railway Company as of December 31, 1920 (Record, p. 202). At a later date, that is, in May, 1921, the Plan was modified so as to eliminate the $9,400,000 payment to General Mortgage bondholders (Record, p. 210), but no one suggested then the reduction of the payments tot be made by the Reading Coal Company or by the New Coal Company. Indeed, it was evident then that to reduce further or to eliminate the payments to be made to the Holding Company by the Reading Coal Company, the New Coal Company or the Holding Company's stockholders, would have served only to inflame and exaggerate the controversy between the preferred and common stockholders by increasing the value of the subject-matter of the controversy.

Thus the fact is that the payments to be made to the New Railway Company by the Reading Coal Company and by the New Coal Company were, as stated in the answer of the Holding Company (Record, p. 163), when the Original Plan was filed, adequate for the requirements of the Holding Company.

Without imposing new and unnecessary burdens to provide the cost of new and unnecessary financing, the Modified Plan and decree (a) redistribute existing burdens between the New Railway Company and the Reading Coal Company approximately in proportion to their relative ability to bear them; (b) apportion to the New Railway Company property the earnings and income of which, during the past ten years and after allowing for adjustments incident to the Plan and the Decree, have been several times the interest on the General Mortgage bonds, leaving an ample margin for dividends; (c) apportion to the Reading Coal Company properties the average annual earnings of which for five years past have been more than four times the interest charges on the $25,000,000 mortgage, leaving a handsome margin for additions, betterments, improvements and for dividends; (d) provide both companies ample working capital; (e) give the stockholders of the Holding Company an opportunity to liquidate gradually their holdings in one company or the other, and thus limit their losses.

The control of the Reading Coal Company will pass immediately from the Holding Company to the nominees of the District Court. The stockholders of the Holding Company will, however, have a reasonable opportunity to sell either the stock of the Holding Company, or the certificates of interest in the stock of the New Coal Company. Thus it is expected the stockholders of the Holding Company will be enabled to protect themselves from some part at least of the loss which would be inevitable if the stock of the Reading Coal Company or the New Coal Company

were thrown directly upon the market. So great a property as that of the Reading Coal Company cannot, under the peculiar general conditions now existing, and under the peculiar special conditions affecting the Reading coal property, be advantageously sold at this time or in bulk (Record, p. 163). The Plan and Decree give the stockholders the benefit of the hope that they may realize more for the coal property than the Holding Company itself could realize for it in the event of a direct sale (Record, p. 163).

VI

Compliance with the decree will not confer on any one class of stockholders of the Holding Company any benefit to the prejudice of the rights of any other class of stockholders.

In support of this point reference is made to the brief for Reading Company, on the original argument of these appeals, filed in this Court January 9, 1922.

VII

The merger of the Reading Railway Company by the Holding Company, the acceptance of the Constitution of Pennsylvania and the surrender of powers inappropriate for a railroad corporation establish a condition in harmony with the decision of this Court.

As to the combination between the Holding Company and the Reading Railway Company, the decree also is in conformity with the opinion of this Court in 253 U. S. 26.

It had been believed by the Holding Company that the relation between the Holding Company and the Reading

Railway Company, in and of itself, contained no vice, but this Court denied, without opinion, the motion of the Holding Company for permission to retain either the Reading Railway Company or the Reading Coal Company. (*United States* v. *Reading Company*, 253 U. S. 478.) In the absence of any indication from this Court, it was assumed that the objection of this Court was to the control of the Reading Railway Company by the Holding Company acting under a special charter, free from regulation by State and Federal authorities having jurisdiction over railroads, and free conceivably to embark upon a new series of combinations in contravention of the law as determined by this Court. At any rate, it was necessary to get rid of this relation, and in doing so to get rid of the Holding Company as such. It was *functus officio*.

It was very evident, bot.. from a study of the opinion of this Court and from obvious considerations of public interest, that merely to terminate the relation between the Holding Company and the Reading Railway Company by the sale of the stock, or stock and bonds, of the Reading Railway Company owned by the Holding Company, and nothing more, though it might have satisfied the letter, would have in large measure defeated the purpose of the decision of this Court. To do so would have left the Holding Company possessed of railroad rolling stock and floating equipment, of real estate needed for railroad purposes, and of securities giving control over railroads and terminals constituting part of the Reading system. It was obvious that the decree, in addition to terminating the relation between the Holding Company and the Reading Railway Company, after the Holding Company had been stripped of its interest in the Reading Coal Company and the Central Railroad Company and the Wilkes-Barre Coal Company, should also *bring together* into one company the remaining properties of the Holding Company and the Reading Railway Company. The relation between the Holding Company and the Reading Rail-

way Company must be terminated not by separation, but by combination. Otherwise that very position of dependence for rolling stock and floating equipment and for traffic from subsidiary lines, which was clearly in the mind of this Court, in its account of the effect of the reorganization of 1896, as a fundamental vice of the situation then created, would be perpetuated and become irremediable. For the Holding Company to sell the stock of the Reading Railway Company and nothing more would have been to perpetuate the situation which this Court frowned upon, because it would have perpetuated the mutual inter-dependence between the Holding Company and the Reading Railway Company. The Reading Railway Company would have owned the railroad system without adequate rolling or floating equipment or tributary lines. The Holding Company would have owned rolling stock and floating equipment and tributary lines in large part useless to it except in connection with the lines of railroad of the Reading Railway system.

The shares of stock and bonds of the Reading Railway Company held by the Holding Company will by operation of law be extinguished by the merger of the two companies. The other assets of the Holding Company and of the Reading Railway Company include besides lines of railroad, rolling stock, real estate, etc., the entire capital stock of Reading Iron Company and stocks and bonds of and claims against various railroad companies and terminal companies carried on the books at $71,057,130.01. (Record, p. 200.) The names of these companies and the amounts of the securities transferred to the Holding Company at the time of the reorganization in 1896 are set forth in the Old Record at pages 1298-1300. The assets of the Holding Company and of the Reading Railway Company not otherwise disposed of, by force of the Decree or for some other reason, will automatically become the property of the New Railway Company.

It would have been possible to effect the termination of the relation, and the combination of the assets, thus clearly indicated as necessary in order to comply with the spirit as well as the letter of the opinion of this Court in 253 U. S. 26, by way of consolidation, merger or sale from one company to the other. In fact, a merger of the Reading Railway Company by the Holding Company is contemplated. Whatever method was adopted, it was obvious that the resulting company must be a Pennsylvania railroad corporation having the powers and subject to the restrictions and regulations governing such a corporation. This the decree effects.

The Holding Company had outstanding capital stock of the par amount of $140,000,000, of which $70,000,000 is preferred stock and $70,000,000 common stock (Record p. 157). It had outstanding $93,269,000 of General Mortgage bonds as to which the Reading Coal Company was co-obligor with it (Record p. 157) and other bonds and obligations to the amount on December 31, 1919, of $38,279,315.28 (Record p. 115).

It was the Holding Company's securities which were outstanding in the hands of the public. Any Plan which had undertaken to disturb the outstanding stock of the Holding Company, the outstanding General Mortgage bonds and the other bonds of or guaranteed by the Holding Company would have involved a vast underwriting expense and, in all probability, grave loss to security holders of some or all classes. The Plan of having the Holding Company merge the Reading Railway Company and then reform and transform itself into an operating railroad company pure and simple seemed best adapted to avoid disturbance of outstanding securities.

Section 2 of Article Ten of the General Mortgage (Old Record, p. 1734) permits any lawful consolidation or merger of the mortgagor companies, i. e., the Holding Com-

pany and the Reading Coal Company or either of them, with each other *or with any other corporation,* or any conveyance and transfer subject to the continuing lien of the General Mortgage of all the mortgaged and pledged premises of the Holding Company or of the Reading Coal Company, or of the property of the Reading Railway Company as an entirety to some corporation lawfully entitled to acquire it, provided that such consolidation, merger or sale shall not impair the lien and security of the General Mortgage or any of the rights or powers of the Trustee or of the bondholders thereunder, and that the payment of the principal and interest of the bonds shall be assumed by every corporation formed by such consolidation or merger or purchasing as aforesaid. This provision expressly permits the merger feature of the Modified Plan and of the decree of the District Court.

The brief submitted on behalf of the Insurance Companies upon the first argument of these appeals erroneously states (p. 3) that under the Plan the Holding Company is to retain its charter. This Court has called attention to the fact that the Reading Company is a holding company having a special "omnibus" charter entitling it to engage in, or control, almost any business other than that of a bank of issue (Record, pp. 8, 20). It is not a common carrier and is not subject to regulation by Federal or State authorities having jurisdiction over railroads (Record, p. 157). It is of the very essence of the Plan, of the Government's consent and approval of it, and of the Decree of the Court below, that the Reading Railway Company shall be merged into the Holding Company and that the latter shall cease to be a holding company, surrender its extraordinary powers, and become a railroad company in all respects subject to the regulation of State and Federal authorities as a common carrier (Record, pp. 43, 277).

Under its charter the Holding Company is empowered

> "* * * to merge or consolidate, or unite with the said company the improvements, property and franchises of any other company or companies, on such terms and conditions as the said company may agree upon; * * *" (Record, p. 193).

The Pennsylvania Act of 1856 provides for the surrender of charter powers, if the stockholders consent and a court of common pleas approve. Said Act is as follows:

> "Section 1. *Be it enacted by the Senate and House of Representatives of the Commonwealth of Pennsylvania in General Assembly met, and it is hereby enacted by the authority of the same,* That it shall be lawful for any court of common pleas of the proper county to hear the petition of any corporation under the seal thereof, by and with the consent of a majority of a meeting of the corporators, duly convened, praying for permission to surrender any power contained in its charter, or for the dissolution of such corporation; and if such court shall be satisfied that the prayer of such petition may be granted, without prejudice to the public welfare, or the interests of the corporators, the court may enter a decree in accordance with the prayer of the petition, whereupon such power shall cease or such corporation be dissolved: *Provided,* That the surrender of any such power shall not in any wise remove any limitation or restriction in such charter; and that the accounts of the managers, directors or trustees of any dissolved company shall be settled in such court, and be approved thereby; and dividends of the effects shall be made among any corporators entitled thereto, as in the case of the accounts of assignees and trustees: *Provided further,* That no property devoted to religious, literary, or charitable uses shall be diverted from the objects for which they were given or granted: *Provided,* That the decree of said court shall not go into effect until a certified copy thereof be filed and recorded in the office of the secretary of the commonwealth." (Laws of Pennsylvania, 1856, p. 293, No. 308.)

The Pennsylvania Act of 1874 provides for acceptance of the Constitution of the State of Pennsylvania if the stockholders consent. Said Act is as follows:

> "Section 1. *Be it enacted, etc.,* That it shall be the duty of the board of directors of any railroad, canal or other transportation company in existence on the first day of January, one thousand eight hundred and seventy-four, desiring to accept of the provisions of the seventeenth article of the constitution of the state, adopted on the sixteenth day of December, one thousand eight hundred and seventy-three, to file in the office of the secretary of the commonwealth a certificate in writing, signed by the president and secretary, and attested by the corporate seal of the company, stating that at a regular or special meeting of said board of directors a resolution, in pursuance of the consent of the stockholders, was adopted, accepting of all the provisions of said article; and all the powers and privileges, and the limitations and restrictions mentioned therein, shall be deemed and taken for all purposes to apply to said corporation; the said certificate shall be recorded in the office of the secretary of the commonwealth, in a suitable book to be by him kept for that purpose.
>
> "Section 2. No such certificate shall be made by the officers aforesaid, without the consent of the stockholders of the corporation, to be obtained by an election to be held in the same manner as prescribed by law for increasing the capital stock of a corporation." (By the consent of a majority of the stockholders.) (Laws of Pennsylvania 1874, p. 275, No. 157.)

Evidently these matters must be laid before the stockholders for their approval, as the decree provides (Record, p. 297).

After such action the New Railway Company formed by the merger will have no powers except those granted to railroad companies incorporated under the general laws of Pennsylvania.

Under the law of Pennsylvania whenever there is a union of two or more corporations, the resulting corporation is a new corporation, distinct from any of the original corporations. This is true whether the union be called a merger or a consolidation; the two terms are interchangeable. *Lauman* v. *The Lebanon Valley Railroad Company,* 30 Pa. St. 42; *Dalmas* v. *Philipsburg & Susquehanna Valley Railroad Company,* 254 Pa. St. 9; *Pennsylvania Utilities Company* v. *Public Service Commission,* 69 Pa. Sup. Ct. 612.

The case of *Lauman* v. *The Lebanon Valley Railroad Company,* 30 Pa. St. 42, was a bill to enjoin The Lebanon Valley Railroad Company from merging with the Philadelphia and Reading Railroad Company, under a special Act of Assembly which gave them power to merge. The Court said, on page 45:

> "This is called a merger of the Lebanon corporation into the other; but such a merger is a dissolution, destroying the actual identity of both, while the legal identity of one of them is preserved."

In the case of *Dalmas* v. *Philipsburg & Susquehanna Railroad Company,* 254 Pa. St. 9, the Court discussed merger under various acts, including the Merger Act of 1865. An interpretation of the word merger as used in these acts passed both before and after the Charter of the Reading Company is an aid in the construction of the legislative intention in the use of the words "merge" and "consolidate" in that Charter. The lower court (its opinion was adopted by the upper court, which affirmed the decision without an opinion), said, on page 15:

> "When two or more corporations merge, the presumption is that all of the property of each constituent company is transferred to and becomes the property of the new company, and that from the time of the completion of said merger the constituent companies cease to exist so far as the terms of

> the act of assembly, under which said merger is effected, preserve their existence; and in order to overcome this presumption there must be a saving clause in the merger proceedings. No such saving clause appears in this bill."

There is no such saving clause in the Charter of the Holding Company (Record p. 189).

In the case of *Pennsylvania Utilities Company* v. *Public Service Commission,* 69 Pa. Sup. Ct. 612, the Court cites *Lauman* v. *The Lebanon Valley Railroad Company* with approval in discussing the Merger Act of 1909, Pennsylvania Laws, p. 408, No. 229, which provides:

> "Section 1. Be it enacted, &c., That it shall be lawful for any corporation, now or hereafter organized under the provisions of any general or special act of Assembly authorizing the formation of any corporation or corporations, to merger its corporate rights, franchises, powers, and privileges with and into those of any other corporation or corporations transacting the same or a similar line of business, so that by virtue of this act such corporations may consolidate, and so that all the property, rights, franchises, and privileges then by law vested in either of such corporations, so merged, shall be transferred to and vested in the corporation into which such merger shall be made."

The Court said, page 618:

> "It is clear the ultimate effect of this act is to provide a method of incorporation, and, as individuals are associated to form a corporate entity, so two or more corporations may be associated to form a single corporate entity. Upon consolidation thereunder the constituent companies are deemed dissolved and their powers and faculties to the extent authorized are vested in the merged company as a new corporation. It is an entity entirely distinct from that of its constituents. It draws its life from the act of consolidation. The fact that to ascertain the powers and faculties of the new

company you must be referred to what existed in the old companies does not affect this result * * *".

The Holding Company will thus be deprived, by the decision of this Court, and the execution of the Plan, of its properties, its corporate powers, its corporate existence even. Though the proceedings take the form of a merger by the Holding Company of the Reading Railway Company, a new corporation will result from these proceedings, and that not a holding company but a railroad company.

Having regard then to the purposes for which it was formed, or reformed, in 1896, to its status and its corporate history as a holding company organized and operated (in the words of Mr. Justice CLARKE—Record, p. 9) "for producing, purchasing, and selling coal and for transporting it to market" through the railroad and coal companies as its agents or instrumentalities, "the mining and transportation departments of its business"; having regard also to the utter disintegration of this business which the decree directs and the Plan effects, and to the termination of the corporate powers and the very corporate existence of the condemned holding company; it is apparent that the decree directs and the Plan effects a very complete and practical dissolution of the Holding Company.

VIII.

The Modified Plan and the decree properly avoid unnecessary disturbance of outstanding securities.

A principal advantage of the particular Plan adopted was that it involved the least possible disturbance of existing securities. This is a consideration at all times of prac-

"* * * In view of the considerations we have stated we leave the matter to the court below to work out a compliance with the law without unnecessary injury to the public or the rights of private property."

IX

As to the combination between the Holding Company and the Central Railroad Company, the decree also is in conformity with the opinion of this Court.

This Court held the control by the Holding Company of the Central Railroad Company to be unlawful, and referred to the acquisition by the Holding Company of the stock of the Central Railroad Company, as follows (220 U. S. 57):

> "Again, when in 1901 a rivalry, imaginary or real, arose for the control of the Central Railroad Company, the Holding Company, regardless of the law, did not hesitate to purchase control of this great competing anthracite coal carrying system with its extensive coal owning and mining subsidiary. This acquisition placed the Holding Company in a position of dominating control not only over two great competing interstate railroad carriers but also over two great competing coal companies, engaged extensively in mining and selling anthracite coal, which must be transported to interstate markets over the controlled interstate lines of railway.
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> * * * * * * * * *
>
> "For flagrant violation of the first and second sections of the Anti-Trust Act, the relations between the Reading Company, the Reading Railway Company and the Reading Coal Company and between these companies and the Central Railroad Company of New Jersey must be so dissolved as to give to each of them a position in all respects indepen-

dent and free from stock or other control of either of the other corporations."

The opinion of this court further held (253 U. S. 64) that as to the Holding Company and the Central Railroad Company the decree of the District Court must be reversed and the cause remanded with directions to enter a decree dissolving the combination of the Holding Company, and the Central Railroad Company, with such provision for the disposition of the shares of stock of that company held by the Holding Company, "as may be necessary to establish the entire independence of that company."

In conformity with the opinion of this court the decree of the District Court provides (Record, pp. 296-297):

"4. The provisions of Section 7 of the Modified Plan shall be consummated as follows:

"a. The Reading Company shall transfer to a Trustee or Trustees to be appointed by this Court (hereinafter called the Jersey Central Trustee), subject to the lien of the Jersey Central Collateral Trust Mortgage dated April 1, 1901 (hereinafter called the Jersey Central Collateral Trust) from Reading Company to The Pennsylvania Company for Insurances on Lives and Granting Annuities, Trustee (hereinafter called the Pennsylvania Company), its right, title and interest in the stock of the Jersey Central.

"b. The Jersey Central Trustee shall hold said right, title and interest in said shares of stock transferred to it as hereinabove provided, subject to the order of this Court. The final disposition of said stock shall be deferred in view of the possible groupings of railroads by the Interstate Commerce Commission under the Transportation Act of 1920, until ordered by this Court. The Court may in its discretion upon its own initiative or upon motion of the United States or the Reading Company without waiting such action by the Interstate Commerce Commission, enter an order for the sale of such

stock, if and when it shall appear that the facts require it, or the situation makes it possible.

"c. The Jersey Central Trustee shall be entitled, and it shall be its duty, to vote or cause to be voted all said shares of the Jersey Central unless otherwise hereafter directed by the Court. The Reading Company is hereby enjoined and restrained from voting upon any such shares of stock of the Jersey Central. The Reading Company shall from time to time direct the Pennsylvania Company, pursuant to the provisions of said Jersey Central Collateral Trust, to execute and deliver to the Jersey Central Trustee or its nominees suitable powers of attorney or proxies to vote upon such shares of stock.

"d. Pending the entry of an order by this Court directing the final disposition of the Jersey Central stock, the Jersey Central Trustee is hereby enjoined and restrained from exercising the voting power on the Jersey Central stock in such a way as to cause any dependence or intercorporate relations between the defendants Reading Company and the Jersey Central, and in particular from voting so that any officer or director of the Reading Company shall be elected an officer or director of the Jersey Central.

"e. Pending the final disposition of the Jersey Central stock the Reading Company shall be entitled to receive all cash dividends on the stock of the Jersey Central. All dividends payable otherwise than in cash which shall be declared by the Jersey Central shall be received and held by the Jersey Central Trustee upon the same terms and conditions as the right, title and interest of Reading Company in the shares of stock in the Jersey Central originally transferred until finally disposed of as may be directed by order of this Court."

The reasons of the District Court for adopting this method of securing the complete independence of the Central Railroad Company from the Holding Company are set forth in the opinion of that court filed May 21, 1921 (Record, pp. 284-286):

"The paragraph of the original Reading Plan numbered eight, which is paragraph numbered seven of the plan as modified in accordance with the agreement between Reading Company and the Attorney General of the United States as of May 12, 1921, contains the only provision in the plan proposed to carry out the mandate of the Supreme Court of the United States which is not agreed to in all of its details by the Reading Company and the Attorney General, and as to this provision of the plan the disagreement relates only to a matter of time.

"The section referred to concerns the disposition by the Reading Company of the stock of the Central Railroad of New Jersey owned by the former, and as to this disposition Reading Company and the Attorney General agree, that the stock shall be transferred to one or more trustees, individual or corporate, to be held and voted under the terms of the trust until sold to a purchaser other than the parties defendant in this cause.

"Reading Company contends that the spirit and the letter of section five of the Interstate Commerce Act, as amended by the Transportation Act of 1920, justifies its prayer that the value of this stock of the Central Railroad Company of New Jersey shall not be subjected to possible sacrifice by a sale until the Interstate Commerce Commission shall adopt a consolidation plan which will designate the several railroads of the East with which the Central Railroad Company of New Jersey may be consolidated, so that assurance may be given to a railroad company purchaser of this stock that the holding of it by such purchaser will not be objectionable.

"The Attorney General has contended that the stock should be placed in the hands of a trustee or trustees under a decree of this Court which shall direct Reading Company to proceed with all due diligence to offer the same for sale within a definite period, and if at the expiration of such period a purchaser has not been found by Reading Company, then upon the application of the Attorney General the Court may decree a sale of this stock at public auction or in such manner as the Court shall then provide.

"The Court is of opinion that because of the provisions of the Transportation Act of 1920 there is presently no prospective purchaser of the Jersey Central stock at a fair price, and so long as the control of the voting power of this stock is taken from Reading Company and lodged with a trustee or trustees, acting under the supervision of this Court, there is full compliance with the mandate of the Supreme Court, which requires that there shall be established entire independence between these two companies, and we are also of opinion there is no good reason why the decree of this Court shall now subject the stock to the possible sacrifice of a forced sale to the detriment not only of the Reading Company but also to the almost equal number of other shareholders of the Jersey Central who are not parties to this record, who have no right to be heard and yet who may be very seriously affected by a decree of this Court ordering at the present time, a forced sale of this majority stock.

"The final decree to be entered herein, therefore, will direct the transfer of the stock of the Central Railroad Company of New Jersey, owned by Reading Company, to such trustee or trustees, individual or corporate, as the Court may name, and shall contain the terms of the trust, which in substance shall provide that the stock shall be voted by the trustee or trustees so that at all times there shall be entire independence of directors and management between Reading Company, as it shall be hereafter merged with Reading Railway Company, and the Central Railroad Company of New Jersey; and that pending a sale of the stock all dividends received by the trustee or trustees upon the same shall be paid to Reading Company or as it shall direct, and that the actual sale of the stock of the Central Railroad Company of New Jersey shall be deferred in view of the possible grouping of railroads by the Interstate Commerce Commission under the Transportation Act of 1920, subject, however, to a provision in the decree that on motion of the United States or other party, or upon the Court's own initiative, that without awaiting such action by the Interstate

Commerce Commission, an order may be entered hereafter, for the sale of such stock, if and when it shall appear to the Court that the facts require it, or the situation makes it possible."

Section 5 of the Interstate Commerce Act, as amended by the Transportation Act, 1920, provides, in part, as follows:

"4. The Commission shall as soon as practicable prepare and adopt a plan for the consolidation of the railway properties of the continental United States into a limited number of systems. In the division of such railways into such systems under such plan, competition shall be preserved as fully as possible and wherever practicable the existing routes and channels of trade and commerce shall be maintained. Subject to the foregoing requirements, the several systems shall be so arranged that the cost of transportation as between competitive systems and as related to the values of the properties through which the service is rendered shall be the same, so far as practicable, so that these systems can employ uniform rates in the movement of competitive traffic and under efficient management earn substantially the same rate of return upon the value of their respective railway properties.

"6. It shall be lawful for two or more carriers by railroad, subject to this Act, to consolidate their properties or any part thereof, into one corporation for the ownership, management and operation of the properties theretofore in separate ownership, management and operation, under the following conditions:

"(a) The proposed consolidation must be in harmony with and in furtherance of the complete plan of consolidation mentioned in paragraph 5 and must be approved by the Commission; * * * *.

"8. The carriers affected by any order made under the foregoing provisions of this section and any corporation organized to effect a consolidation approved and authorized in such order shall be, and they are hereby, relieved from the operation of the 'anti-trust laws', as designated in Section I, of the Act entitled 'An act to supplement existing laws against unlawful restraints and monopolies, and for other purposes,' approved October 15, 1914, and of all other restraints or prohibitions by law, State or Federal, in so far as may be necessary to enable them to do anything authorized or required by any order made under and pursuant to the foregoing provisions of this section."

The decree of the District Court fully complies with the opinion of this Court in that it insures the immediate independence of the Central Railroad Company from the Holding Company by vesting in trustees appointed by the District Court in its decree of June 11, 1921 (Record, p. 313), the right, title and interest of the Holding Company in the stock of the Central Railroad Company, carrying with it the power to vote the controlling shares of the stock of the latter until such time as by further order of the Court the shares of stock might be finally disposed of.

By the decree the trustees so appointed are enjoined and restrained from exercising the voting power on the stock of the Central Railroad Company in such a way as to cause any dependence or intercorporate relations between the Holding Company and the Central Railroad Company, and in particular from voting so that any officer or director of the Holding Company shall be elected an officer or director of the Central Railroad Company.

The final disposition of the stock of the Central Railroad Company was deferred until ordered by the Court in view of the possible grouping of railroads by the Interstate Commerce Commission under the Transportation Act of 1920.

Otherwise the lawful exercise of powers by the Interstate Commerce Commission might have been irreparably interfered with by a final decree of the District Court in this cause, subsequently ascertained to be in conflict with the orders of the Commission to be entered under the Transportation Act of 1920. This provision of the decree was to accord with the action taken by this Court in the case of *United States* v. *Terminal Railroad Association of St. Louis*, 224 U. S. 383. In that case this Court remanded the cause to the District Court with instructions to enter a decree embodying a plan for the reorganization of the defendant companies and indicated specifically certain provisions to be embodied in this plan for reorganization, expressly providing, however (page 412), that

> "the decree should also contain a provision that nothing therein shall be taken to affect in any wise or at any time the power of the Interstate Commerce Commission over the rates to be charged, * * * etc., or any other power conferred by law upon such Commission."

The Court below was cautious, however, to preserve its control over the situation by further order in addition to its control of the voting power of the stock through its trustees, and qualified its postponement of the sale by the latter part of paragraph (b) of section 4 of the decree, in which it provided (Record, p. 296):

> "* * * The Court may in its discretion upon its own initiative or upon motion of the United States or the Reading Company without waiting such action by the Interstate Commerce Commission, enter an order for the sale of such stock, if and when it shall appear that the facts require it, or the situation makes it possible."

X

The disposition of the stock of the Wilkes-Barre Coal Company by the Central Railroad Company establishes the entire independence of the Wilkes-Barre Coal Company from the Central Railroad Company and from the other corporate defendants.

As to the combination between the Central Railroad Company and the Wilkes-Barre Coal Company, the decree also is in conformity with the opinion of this Court. The opinion of this Court affirmed the original judgment of the District Court with reference to the sale by Central Railroad Company of the stock of the Wilkes-Barre Coal Company owned by it, and directed that

> "* * * such disposition shall be made by the decree of the stocks and bonds of the Lehigh & Wilkes-Barre Coal Company, held by the Central Railroad Company of New Jersey, as may be necessary to establish entire independence between these two companies to the end that the affairs of all of these now combined companies may be conducted in harmony with the law."

The decree of the District Court provides (Record, p. 298), in paragraph 8 thereof, as follows:

> "8. The Central Railroad Company of New Jersey shall dispose of all the capital stock of The Lehigh & Wilkes-Barre Coal Company now owned by it to persons or corporations who are not its own stockholders or stockholders in either the Reading Company, the Railway Company or the Coal Company, and who previous to or at the time of purchase shall qualify as purchasers by a duly executed affidavit in one of the forms hereto annexed. * * *"

CONCLUSION

The Decree of the District Court should be affirmed.

Respectfully submitted,

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